

INPUT

STRATEGIC MARKET PERSPECTIVE

Business Operations
Outsourcing
Europe, 1993

Outsourcing Information Systems
Programme - Europe

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BUSINESS OPERATIONS OUTSOURCING

EUROPE, 1993

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Abstract

Most organisations in Europe are either undertaking or considering some form of business re-engineering in order to reduce their costs and improve their effectiveness. While this activity has led to the IT services sector benefiting from the award of major systems integration and IT outsourcing contracts, a wider opportunity has begun to emerge namely business operations outsourcing. Business operations outsourcing is arising out of the desire, evident in many organisations, to outsource entire business functions or processes. The benefits of this approach are increased operational flexibility and increased focus on core business activities.

This report analyses the opportunities for IT vendors in the emerging business operations market. In particular it analyses the type of business activity that organisations expect to outsource, the key characteristics of prime candidates for outsourcing and senior executives' attitudes towards potential vendors.

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Business Operations Outsourcing Europe, 1993

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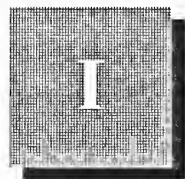
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Introduction

This report is produced as one of a series of executive perspectives in INPUT's Outsourcing Information Service Programme for the computer software and services industry in Europe.

A

Scope and Objectives

IT outsourcing is becoming well-established in Europe. However, it can be a very competitive market and a number of vendors are endeavouring to establish outsourcing services which transcend IT. INPUT calls this type of service "business operations outsourcing." Business operations outsourcing is defined as the contracting out of components, or all, of a business process or function.

One benefit of this form of outsourcing to the client is that it enables the effectiveness and efficiency of a complete business process to be optimised by a single vendor. In the long run, this approach may be more effective than individually optimising the individual supporting elements of a process, for example computer operations.

This report focuses on business operations outsourcing in Europe. The objectives of the report are as follows:

- To identify the current status of business operations outsourcing in Europe
- To identify the types of business function which are being outsourced and being considered for outsourcing
- To identify the characteristics which make a business process appropriate for outsourcing
- To identify examples of business operations contracts in the commercial sector
- To identify vendor selection criteria

- To investigate the perceived business operations capability of a number of named vendors of outsourcing services.

B

Methodology

The research is based on interviews with 39 users and eight vendors. The users interviewed were senior executives within organisations which already use IT outsourcing services. IT managers were not included within the respondents. The breakdown of senior executives interviewed by country is as follows:

- 17 in the United Kingdom
- 13 in France
- 9 in Germany.

Vendor interviews were carried out to identify the nature of business operations services currently offered and to identify specific business operations contracts.

C

Report Structure

Section II consists of the Executive Overview which is a summary of the key conclusions of the study.

Section III analyses the opportunity for business operations outsourcing within Europe. In particular, it focuses on:

- The types of activities being outsourced
- Organisations' motivations for adopting business operations outsourcing
- The characteristics which make a business function a prime candidate for outsourcing
- Potential purchasers' vendor selection criteria
- The perceived level of business operations capability of a number of selected vendors.

Section IV analyses the differing nature of the opportunity and the perceived capability of vendors across each of the United Kingdom, France and Germany.

Section V provides case studies of a number of examples of business operations outsourcing in Europe.

D

Related Reports

Information Systems Outsourcing Competitive Analysis—Europe, 1992

Outsourcing Systems Operations—Europe, 1992-1997

Outsourcing Network Management and Operations—Europe, 1992-1997

Outsourcing Desktop Services—Europe, 1992-1997

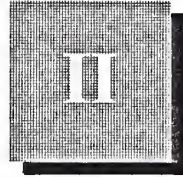
Outsourcing Applications Management—Europe, 1992-1997

Outsourcing Opportunities in Government—Europe, 1993-1998

Information Systems Outsourcing Market—Europe, 1993-1998

Client Satisfaction with IT Outsourcing Services—Europe, 1993

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Executive Overview

A

Business Operations Market Emerges in Europe

The first major business operations contract in Europe was signed between BP Exploration and Andersen Consulting in 1991. In the period following the award of this contract, there was little sign of further activity in the business operations market place.

However, business operations outsourcing is now beginning to emerge as a significant opportunity, valued at \$150 million in Europe in 1993.

Approximately one-third of this market value is accounted for by outsourcing within the public sector in the United Kingdom. In this segment of the market, the traditional IT outsourcing vendors are finding that they must now offer business operations outsourcing or “managed services” in addition to IT outsourcing in order to retain their presence in this market segment. This could also happen in the wider commercial marketplace posing a significant threat to IT outsourcing vendors and systems integration vendors. Accordingly it is important that vendors recognise the nature of the business operations opportunity and the threat to their current business activities from other vendors offering such services.

INPUT's research shows that:

- Administrative functions are prime candidates for business operations outsourcing
- Business operations outsourcing offers an alternative approach to systems integration
- Andersen Consulting and EDS are the early market leaders.

In addition, the business operations market is forecast to grow more rapidly than the IS outsourcing market over the next five years.

B**Administrative Functions are Prime Candidates**

Exhibit II-1 lists examples of current business operations contracts which have been awarded to IT vendors.

EXHIBIT II-1

Examples of Business Operations Contracts

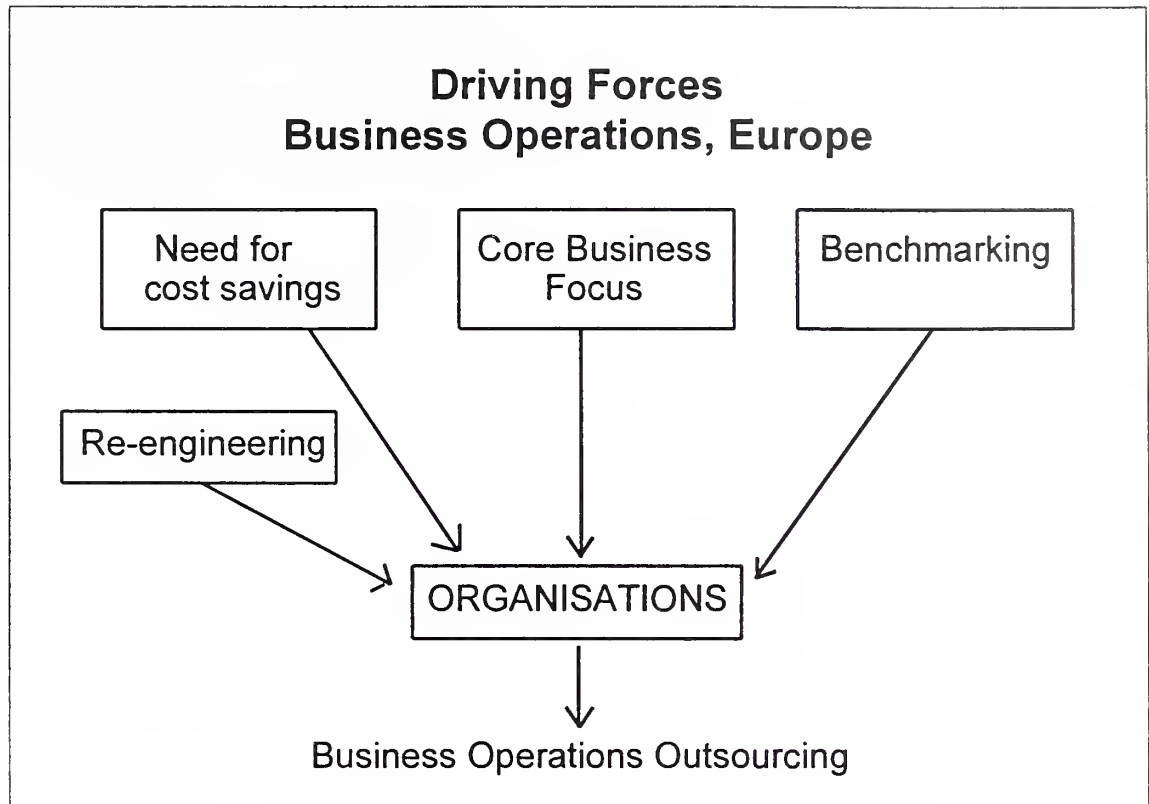
Contract	Vendor
Fulfilment for Time Life books and magazines	EDS
Parking Fine Collection in Seville	EDS
Accounting for BP Exploration	Andersen Consulting
Administration of BP's share register	CMG

Each of these activities involves a considerable administrative workload. For example, EDS' contract with Time Life involves millions of transactions per annum.

However, potential buyers of business operations services indicated that transaction volume was not itself a significant factor in the decision to outsource a business process.

The principal driving forces behind business operations outsourcing are shown in Exhibit II-2.

EXHIBIT II-2



A perceived need for cost reduction is usually a prerequisite for business operations outsourcing, along with a belief that the organisation will be most effective if it concentrates solely on a small number of core activities. Both IT outsourcing and business operations outsourcing have proved themselves very successful in freeing management to concentrate on important business issues rather than day-to-day problem management.

The perception that a business process requires re-engineering to improve its engineering is another driving force. To increase the flexibility of the organisation to react to market changes, companies may decide to outsource the business process rather than re-engineer the process themselves. For example, BP Exploration wished to give Andersen Consulting the scope to re-engineer their accounting function. As a result, they outsourced the entire process to a single vendor, and not just constituent parts of the process such as the IT components.

Traditionally many organisations have been reluctant to acknowledge their failings in any business process. Accordingly it can be difficult for vendors to persuade potential buyers that the effectiveness and efficiency of an existing process could be improved by outsourcing it. One approach to overcoming such objections is to introduce benchmarking, which demonstrates the organisations relative level of capability in business processes and assists in identifying candidates for re-engineering or outsourcing.

The principal characteristics which users perceive increase the probability of a business process being outsourced are shown in Exhibit II-3.

EXHIBIT II-3

Key Characteristics of Target Functions Business Operations, Europe

- High cost/labour-intensive operations
- Variable usage
- Common to many organisations

Organisations are most likely to outsource operations which are labour intensive, particularly if these operations show considerable peaks and troughs of activity. In addition, organisations are more likely to outsource activities which they perceive as commonplace than activities which they perceive to be unique to their own organisation.

It is often argued that organisations will not outsource activities that are a part of their core business and provide them with competitive advantage. However, this appears to be a myth. Organisations are already outsourcing activities which are important sources of competitive advantage. For example, Vauxhall is reluctant to discuss the nature of its Customer Assistance Centre run by EDS, because this business operations contract is a source of competitive advantage.

Since the centre was established, Vauxhall claims “a substantial rise in customer satisfaction as well as an increase in those prepared to recommend Vauxhall products.”

Provided that the client retains the means of establishing policy and direction together with the means to monitor service delivery and manage the vendor, there are probably few activities that cannot be effectively outsourced at the administrative or operational level. Many business operations contracts involve third parties liaising directly with the clients’ customers and suppliers.

C

An Alternative to Systems Integration

Organisations show relatively high propensity to outsource high cost/labour-intensive business processes.

This implies that business operations outsourcing involves transferring responsibility for re-engineering a business process from the client to the vendor. Accordingly the contract between client and vendor becomes a business operations contract as opposed to a systems integration contract or even an applications operations contract.

This means that business operations contracts will often supplant systems integration contracts in a similar manner to applications operations contracts.

Examples of business operations contracts that include significant immediate re-engineering and systems integration activity are EDS' contracts for parking fine administration in Seville and London. Claims administration for an insurance company would be another example. In this case, technologies such as workflow and document image processing could be immediately applied to transform the business process.

Alternatively business operations can be used to pre-empt future systems integration contracts. For example, EDS has a contract with Time Life to provide fulfilment services. At present, the process remains labour-intensive. However, EDS will endeavour to apply technology to the process to improve its efficiency. This will probably entail re-engineering the process and performing a systems integration project at some future date. In this way, EDS has effectively pre-empted the award of a systems integration project. The vendor has also avoided the price competition inherent in a competitive tender for such a project.

Exhibit II-6 lists three possible approaches that vendors can take to business operations outsourcing.

EXHIBIT II-4

Approaches to Business Operations Outsourcing

- Re-engineer process with improved IT support but offer operational service not IT project
- Take on business process with view to subsequent re-engineering
- Extend processing service to wider business process operation

The first two of these approaches have already been discussed. These types of approach are being adopted by organisations such as Andersen Consulting and EDS.

However, there is a third approach that vendors can adopt, namely extending existing processing services. One example of an organisation adopting this approach is CMG. CMG has traditionally offered bureau services for payroll processing and share registration. The company has now extended these services to include business operations capabilities. For example, CMG now provides clients such as BP and Grand Metropolitan with a wide range of share registration services including:

- Shareholder queries
- AGM administration
- Dividend fund administration including scrip dividends
- Administration of lost certificates and shareholder deaths.

CMG is currently considering expanding its share registration services to include a wider range of investor services.

Similarly the company's payroll services have been expanded to include:

- Processing of raw employee data
- Handling employee queries
- Liaison with tax authorities.

D

EDS and Andersen Consulting are Early Market Leaders

The attitudes of senior executives towards the business operations capabilities of IT vendors are listed in Exhibit II-5.

EXHIBIT II-5

Perceived Vendor Capability Business Operations, Europe

- IT vendors perceived to have low levels of capability
- Services vendors favoured over equipment vendors
- EDS & Andersen Consulting perceived to have highest levels of capability

Overall IT vendors are regarded as having low levels of business operations capability. No vendor in this survey averaged a score indicating even moderate perceived capability across France, Germany and the United Kingdom. The highest individual ratings were both in France and were awarded to EDS and GSI.

Services vendors are more highly regarded than equipment vendors in this marketplace. IBM received consistently low ratings across France, Germany and the United Kingdom. The only equipment vendor to outscore services vendors in any country was SNI in Germany.

However, this perception may change as the business operations market matures. At a similar stage in the development of the IT outsourcing market in Europe, equipment vendors were regarded as much less suitable partners than professional services vendors. This has not prevented organisations such as Axone and IBM ISL subsequently becoming successful in the outsourcing market. Nevertheless, the services companies have established an early lead in this market.

At present the leading vendors in business operations outsourcing in the public sector in the United Kingdom are Capita Group and CSL. CSL has recently been acquired by Touche Ross to establish a "managed services" business unit. In the future, this unit may extend its targeting outside the public sector and offer business operations services for accounting departments in competition with Andersen Consulting.

In the commercial sector, the market leaders in business operations outsourcing are EDS and Andersen Consulting. Andersen Consulting now has four major business operations outsourcing contracts, including the accounting functions of three oil companies.

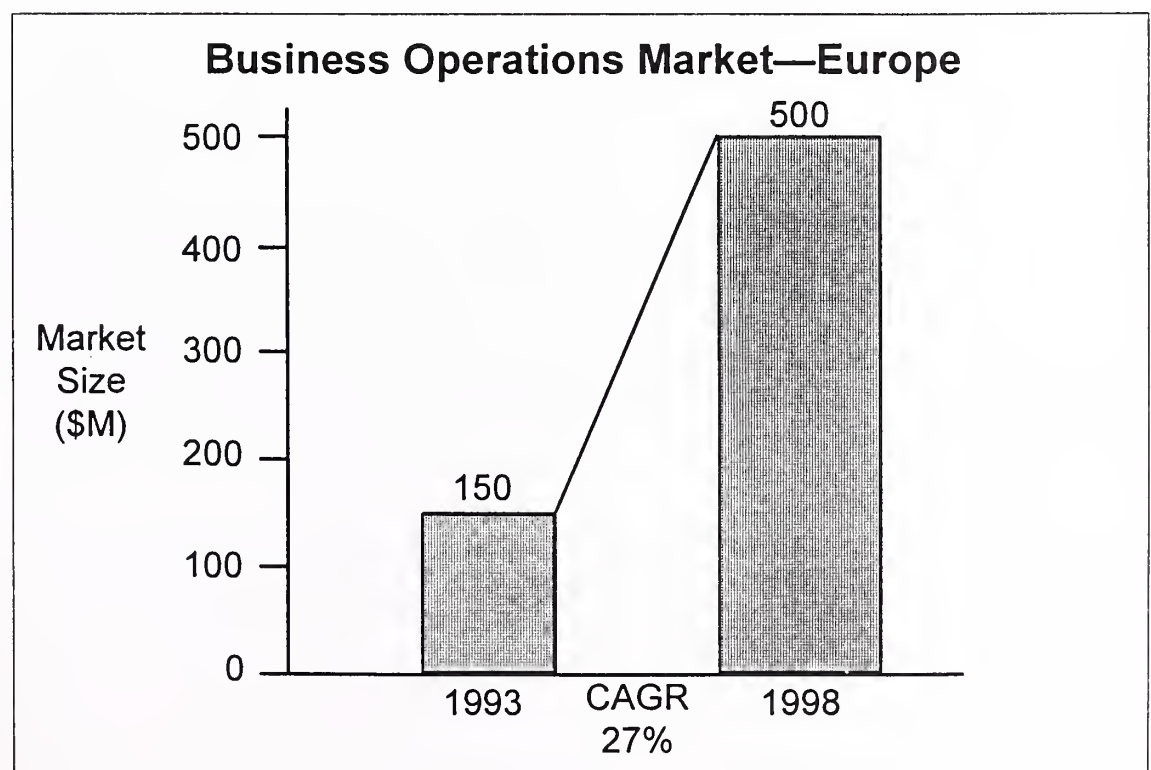
EDS has a similar number of business operations contracts in Europe including two parking fine administration systems and fulfilment services for Time Life. There is also believed to be a business operations component within the DVOIT agency currently being acquired from the U.K. government by EDS.

E

Business Operations Market Forecast to Grow at 27% Per Annum

Exhibit II-6 provides a forecast for the business operations market in Europe.

EXHIBIT II-6



A more detailed breakdown is provided in Exhibit II-7.

EXHIBIT II-7

Business Operations Market Europe

Sector	1993 \$M	1998 \$M	CAGR (%)
U.K. local government	50	240	37
Rest of market	100	260	21
Business Operations - Total	150	500	27
IS Outsourcing	3,300	8,600	21

This shows that the major source of growth over the next five years will be local government in the United Kingdom.

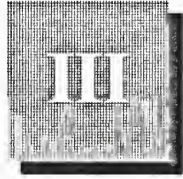
The introduction of compulsory competitive tendering means that councils must introduce competition by 1st October 1996 for the following business functions:

- Finance (25% of activity)
- Corporate administration (15% of activity)
- Personnel (25% of activity).

This implies a requirement to go out to tender by October 1995.

Other business functions such as housing administration and legal services are subject to even earlier deadlines for the introduction of competition.

Business operations outsourcing in the commercial sector will show lower levels of growth, with initial growth mainly centred around the U.K. market. Accordingly the business operations market is expected to remain much smaller than the IS outsourcing market throughout the forecast period. Nonetheless, in the very long term, business operations has considerably higher market potential.



Business Operations—The Future of Outsourcing?

A

Logistics & Accounting Exhibit Business Operations Potential

IT outsourcing is becoming an extremely competitive market. Consequently, a number of vendors, for example EDS and Andersen Consulting, are actively endeavouring to extend the scope of their outsourcing activities beyond information systems into additional business functions. INPUT calls this form of outsourcing “business operations outsourcing.”

Business operations outsourcing is becoming attractive to organisations for a number of reasons, namely:

- The current emphasis being placed on adopting a core business focus and outsourcing secondary and support activities
- The need for organisational flexibility
- The desire to take a more holistic approach to business process improvement.

In particular, buyers of information services have found that contracting out IT projects or functions does not always produce the anticipated business benefits. It can be argued that significant benefits are more likely to be achieved if the supplier focuses on optimising delivery of the overall business function and not just its IT aspects.

However, organisations have been involved in outsourcing business functions for decades. One of the principal issues is to identify those business functions where

- IT vendors can make a significant contribution
- Potential buyers consider IT vendors to be a suitable choice.

Clearly there is no obvious advantage in an IT vendor supplying

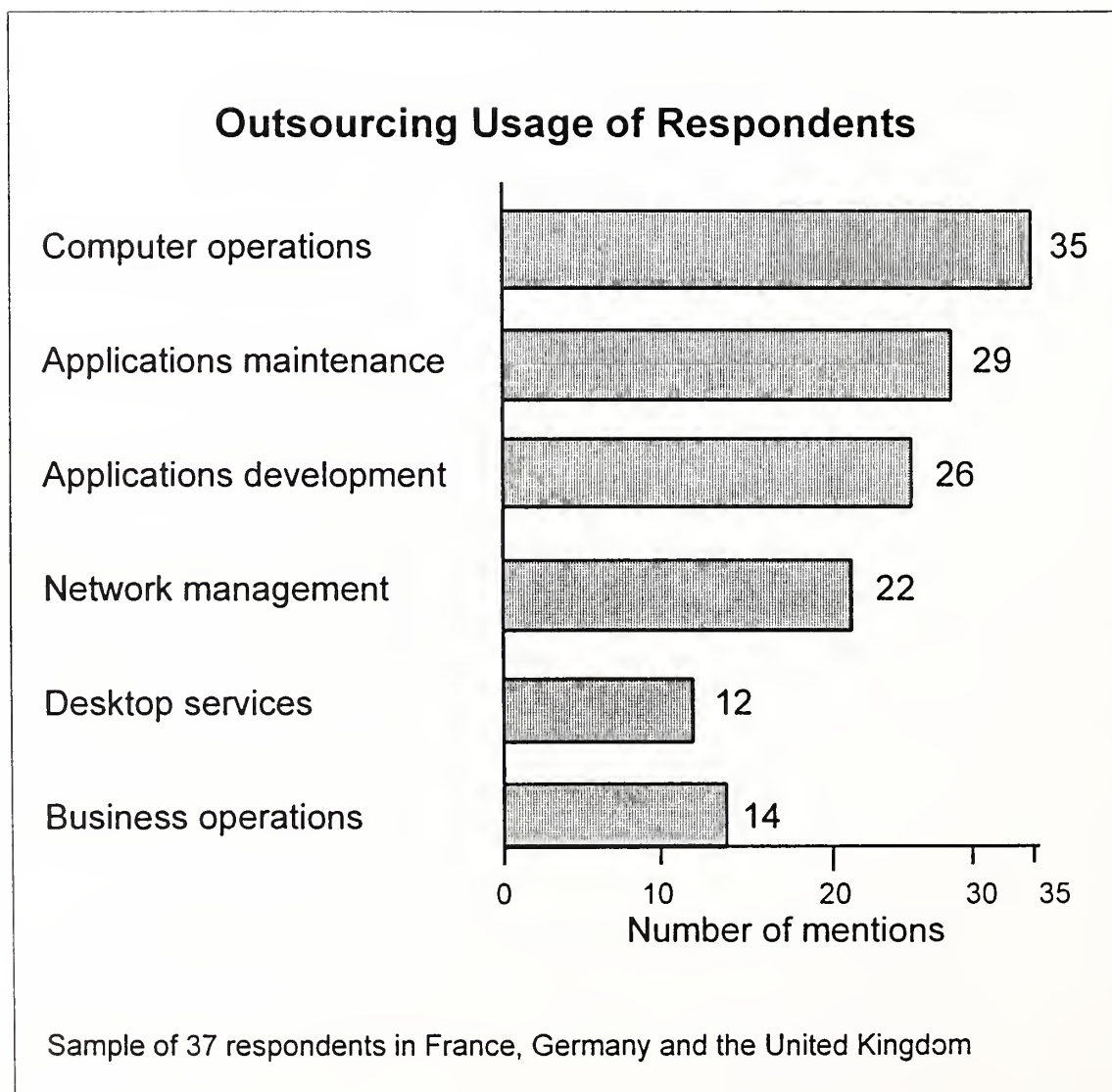
- Office cleaning services
- Catering services
- Grounds maintenance.

Nonetheless, some vendors may wish to do so as part of their targeting of building facilities management, and as a possible extension of IT infrastructure management services.

This report excludes discussion of services of this type and focuses on opportunities where IT is an important component of the service supplied or where IT can make a significant contribution to the effectiveness or efficiency of the business function.

Thirty seven respondents were interviewed about their attitudes towards business operations outsourcing. Each of their organisations already used some form of IS outsourcing. The level of usage of outsourcing services by these respondents is shown in Exhibit III-1.

EXHIBIT III-1



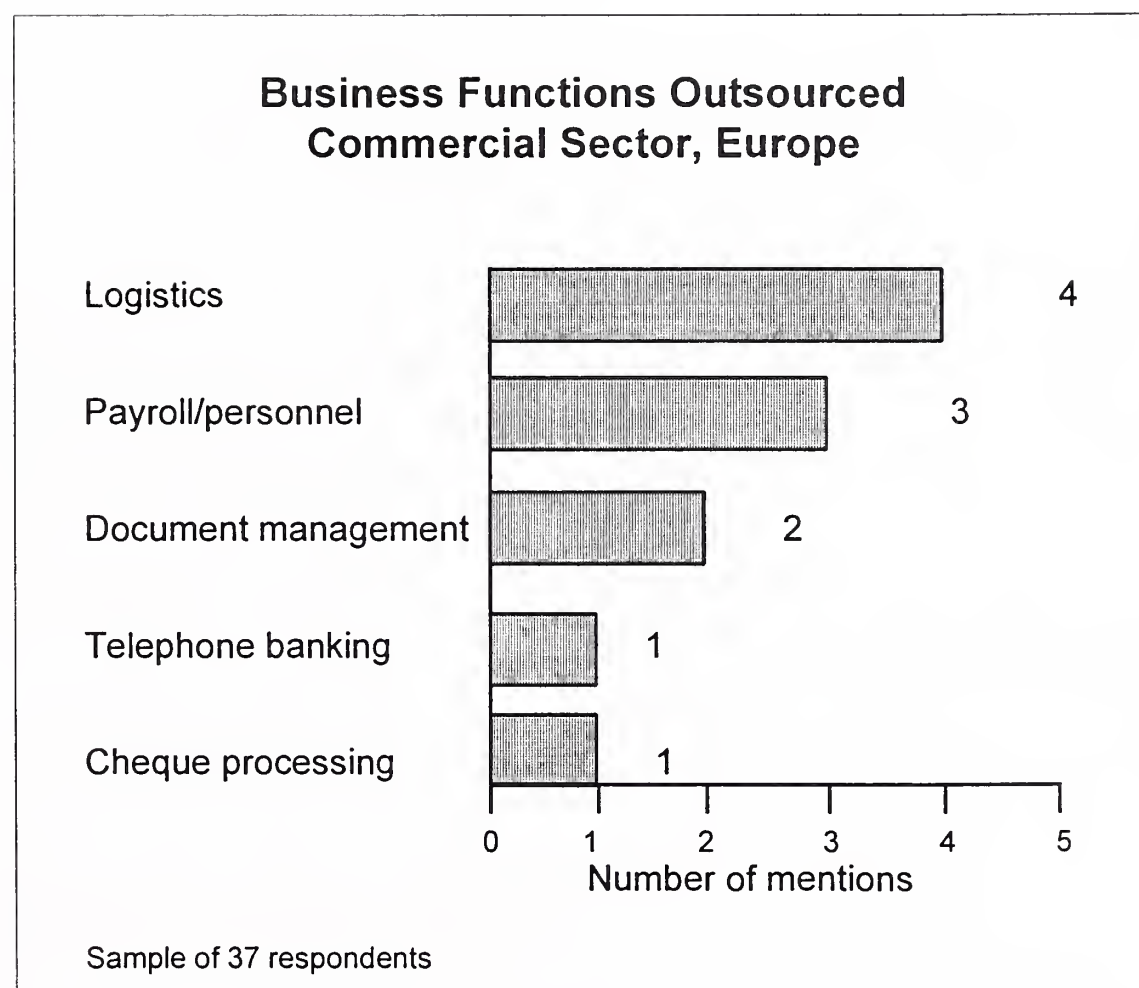
Despite the limited penetration of business operations outsourcing by IT vendors, nearly 40% of respondents perceive that they already undertake some form of business operations outsourcing.

Accordingly, many organisations are familiar with the concept and are not averse to outsourcing in principle.

Business operations outsourcing is becoming commonplace in the government sector in the United Kingdom, where it is generally referred to as "managed services." This opportunity is not discussed in this report since it is already analysed in the report "Outsourcing Opportunities in Government—Europe, 1993-1998." Instead this report focuses on business operations opportunities in the commercial sector.

The business functions that respondents in the commercial sector perceived to be already outsourced by their organisations are listed in Exhibit III-2.

EXHIBIT III-2



Logistics is a major business operations opportunity. In this survey, the aspects of logistics outsourced by organisations ranged from customer delivery to purchasing and stockholding.

This may not be an opportunity that many IT vendors will consider themselves well-placed to address. However, logistics is an area where effective use of IT is critical, and there are already some examples of logistics contracts with IT vendors.

For example, EDS

- Has one contract in Europe to distribute product from its warehouse in Eindhoven on behalf of a PC manufacturer. TPD manages the inventory, country-specific tailoring and shipping to resellers. TPD also provides a multilingual help-desk on behalf of this client.
- Manages fulfilment on behalf of Time Life books in Europe.

Accounting services is another significant opportunity. Andersen Consulting's contract to perform BP Exploration's accounting activities in Aberdeen is the best example of this type of business operations outsourcing in Europe. However, respondents to this survey stated that their organisations were outsourcing components of the accounting function such as payroll and debt collection.

Organisations are apparently prepared to outsource critical business activities to maintain high levels of flexibility. One organisation had recently introduced a 24-hour telephone banking service. Such a service is a key part of the organisation's future business strategy. However, because the initial service was a trial, which could fail as well as succeed, the organisation decided to outsource the service delivery.

Exhibit III-3 shows the profile of contract lengths for existing business operations contracts.

EXHIBIT III-3

**Contract Length
Business Operations, Europe**

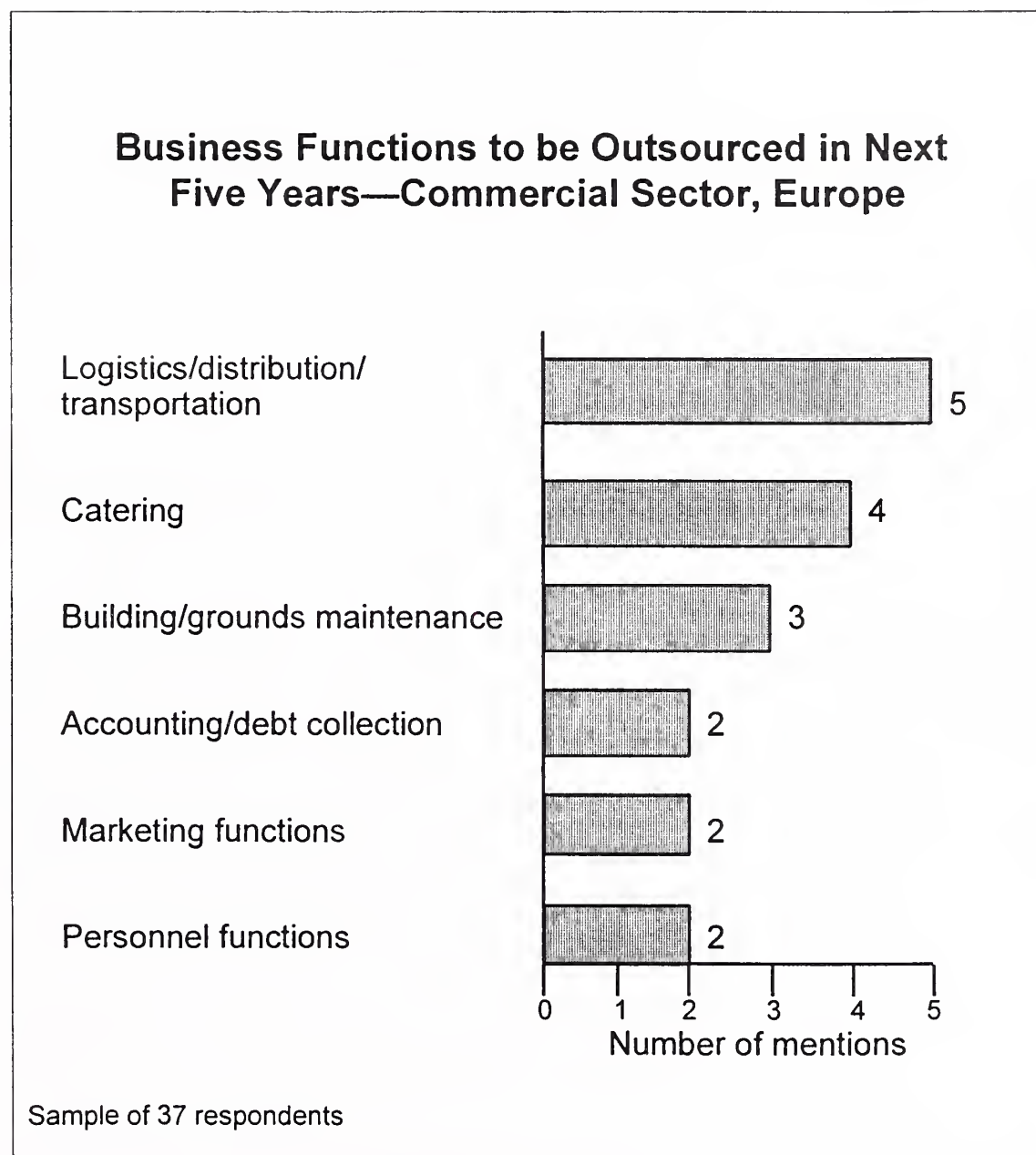
Period (years)	Number of Contracts
<1	3
3-5	8
>5	1
Average	3.75

Sample of 12 respondents

The average length of a business operations contract is similar to that of IS outsourcing contracts. However, the profile is significantly different. A quarter of the business operations contracts are for a year or less.

Exhibit III-4 lists the business operations outsourcing intentions of respondents in the commercial sector.

EXHIBIT III-4



This exhibit includes business functions which have little apparent relevance to IT vendors. These activities include:

- Catering
- Buildings and grounds maintenance.

Other activities of this type mentioned include:

- Security
- Waste disposal.

However, some IT vendors will decide to include elements of these predominantly blue-collar activities who business operations contracts. This will particularly apply to vendors who decide to include building services within an overall infrastructure management offering.

Logistics remains a major business operations opportunity. The scope of future logistics outsourcing mentioned by respondents ranged from all distribution activities including warehousing to elements of rural distribution only.

The remaining functions listed in Exhibit III-4 are all white-collar, staff functions. Many organisations are endeavouring to empower individual business units and to reduce their dependence on centralised, staff functions. Outsourcing these functions is one way of reducing this dependence and providing more flexible manning of such functions.

B

Business Operations Candidates are High Cost and Labour Intensive

The previous section identified some business functions which are candidates for business operations outsourcing. However, this is not an exclusive list of opportunities. To identify additional opportunities, vendors need to identify potential buyers' motivations for outsourcing business functions.

The principal reasons given by respondents for outsourcing business functions are listed in Exhibit III-5.

EXHIBIT III-5



The desire to adopt a core business focus is a significant factor. However the motivation behind this focus is a very strong requirement to reduce costs, and overhead costs in particular.

Initially the main targets for outsourcing are activities which are perceived to have little strategic importance. However this may turn out to be too simplistic a view in the long term. Provided the buyer can maintain control of the activity, there should be a strong motivation to outsource any activity where improved value for money and flexibility can be obtained by outsourcing, whether the activity is strategically important or not.

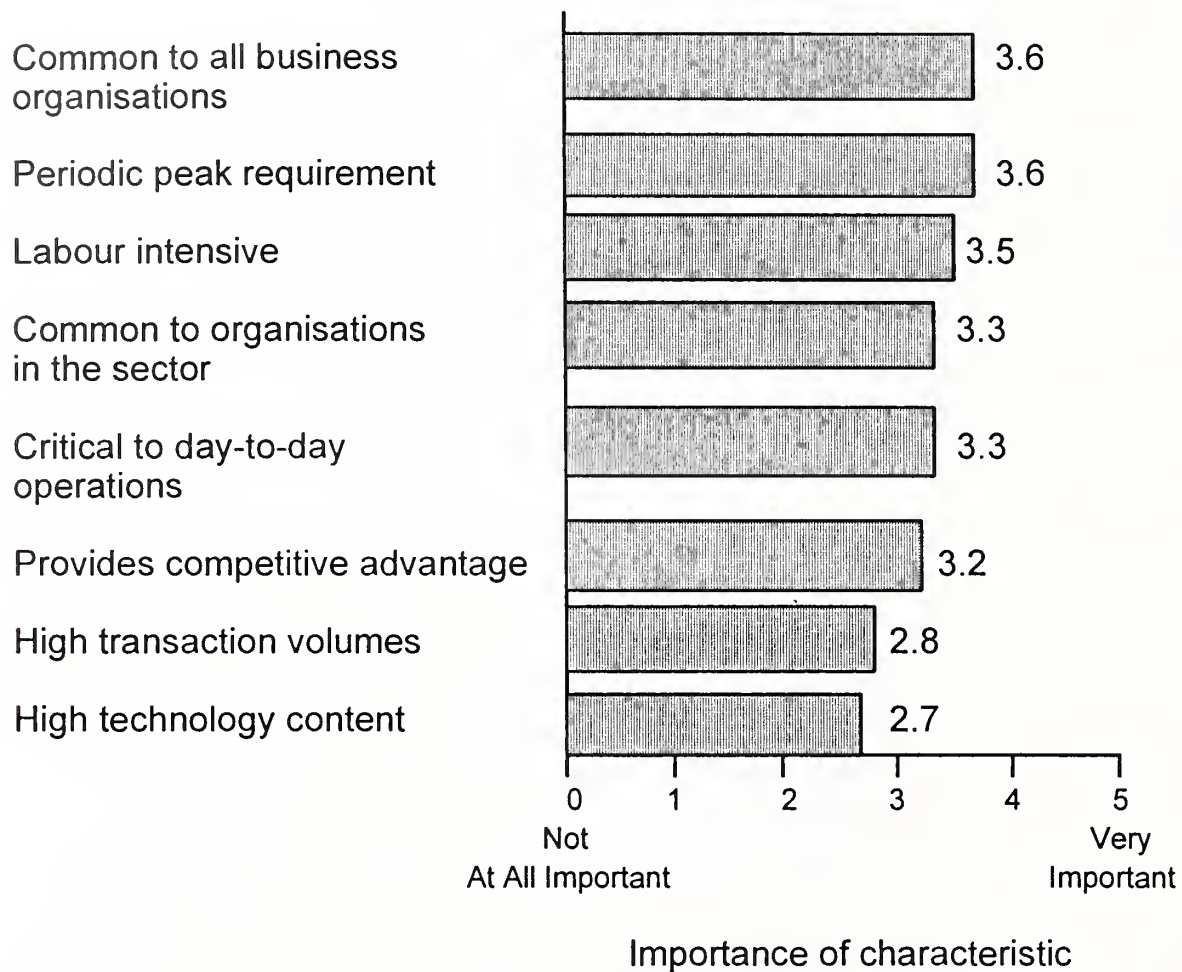
Respondents were also asked to rate the importance of each of a list of characteristics which might make a business operation a candidate for outsourcing. The resulting ratings are listed in Exhibit III-6.

Again buyers anticipate that they are more likely to outsource a business function that is common to all business organisations rather than one that is common to their industry sector or unique to their organisation.

Labour intensive activities are potential candidates for outsourcing, particularly if the requirement for the activity is seasonal or shows considerable variation over time.

EXHIBIT III-6

Principal Characteristics of Functions to be Outsourced Europe



Sample of 36 respondents - France, Germany and the U.K.
Standard error = 0.2.

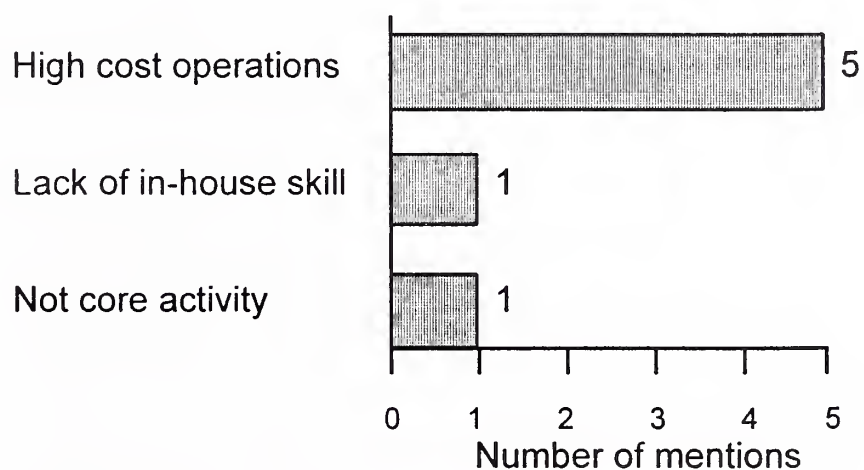
From the viewpoint of IT vendors, it is important to note that the respondents showed no increase in propensity to outsource activities with a high technology content nor which involved high transaction volumes.

The manpower intensity of the process and its current cost are more important determinants of business operations outsourcing.

The cost element is again emphasised in Exhibit III-7.

EXHIBIT III-7

Other Characteristics of Functions to be Outsourced Europe



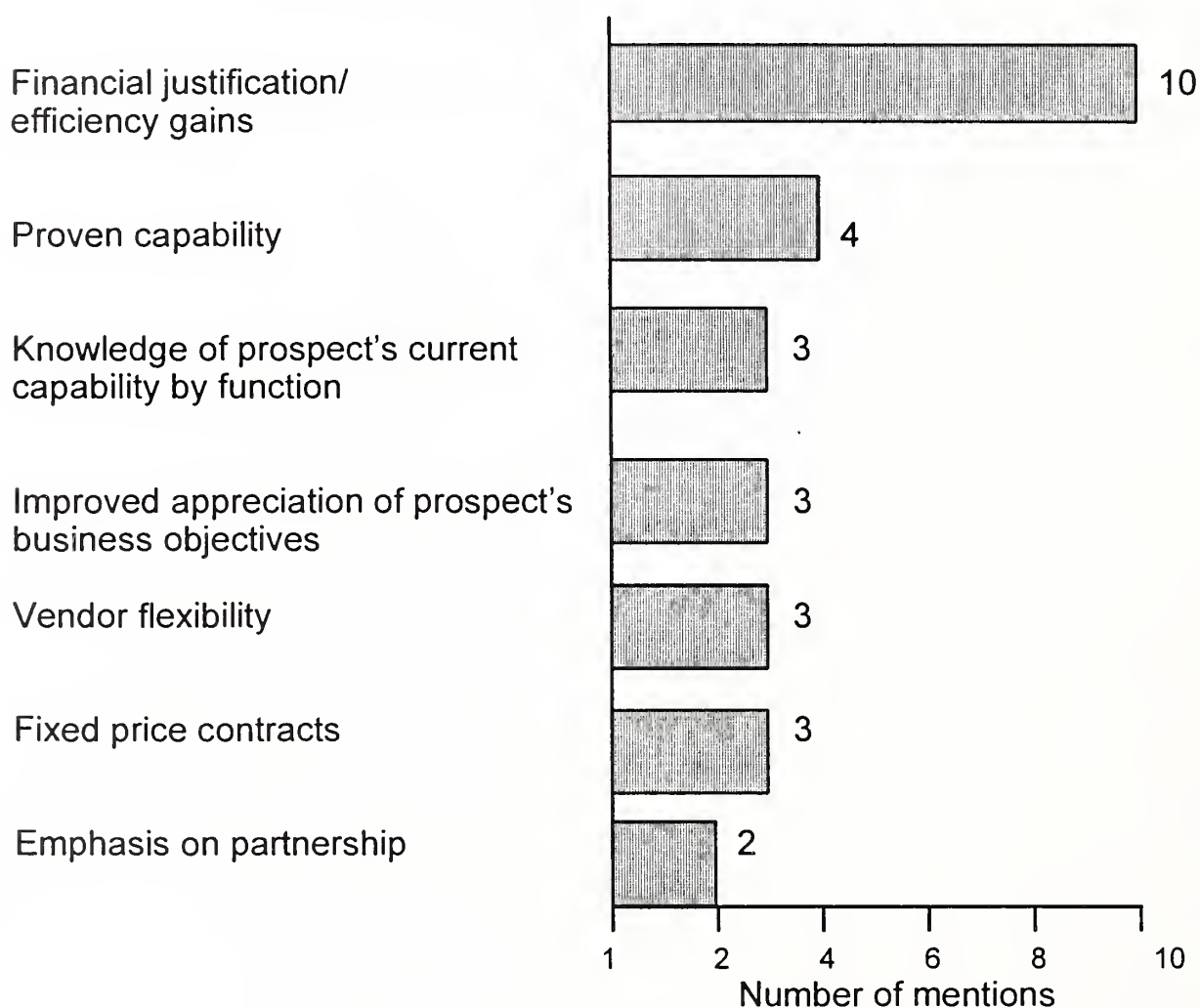
Sample of 37 respondents in France, Germany and U.K.

This shows additional important attributes of business operations candidates. Business functions which are perceived to account for a significant proportion of the organisation's cost base and where the organisation perceives it has no particular cost advantage are prime candidates for outsourcing.

Exhibit III-8 lists the principal factors that buyers perceive will increase the appeal of business operations outsourcing.

EXHIBIT III-8

Factors that Increase the Appeal of Business Operations Outsourcing



Sample of 37 respondents

Obviously vendors need to demonstrate the efficiency gains that the prospect will receive from adopting business operations outsourcing. Vendors also need to demonstrate their own capabilities to their prospects' satisfaction.

However, there is another factor which could be extremely persuasive, namely benchmarking. Ideally, the vendor needs to be able to present objective comparisons of the relative effectiveness and efficiency in a particular process of:

- The prospect
- The prospect's main competitors
- The vendor
- Leading organisations.

This would potentially enable the vendor to present a very strong case for business operations outsourcing.

One criticism of suppliers of IT outsourcing is that they are insufficiently pro-active. Instead of emphasising the importance of the partnership between vendor and user, vendors sometimes see the relationship in more contractual terms.

In business operations outsourcing, it is especially critical that vendors show flexibility in responding to the needs of their clients. It is also important that vendors continue to improve the effectiveness and the efficiency of the processes for which they are responsible.

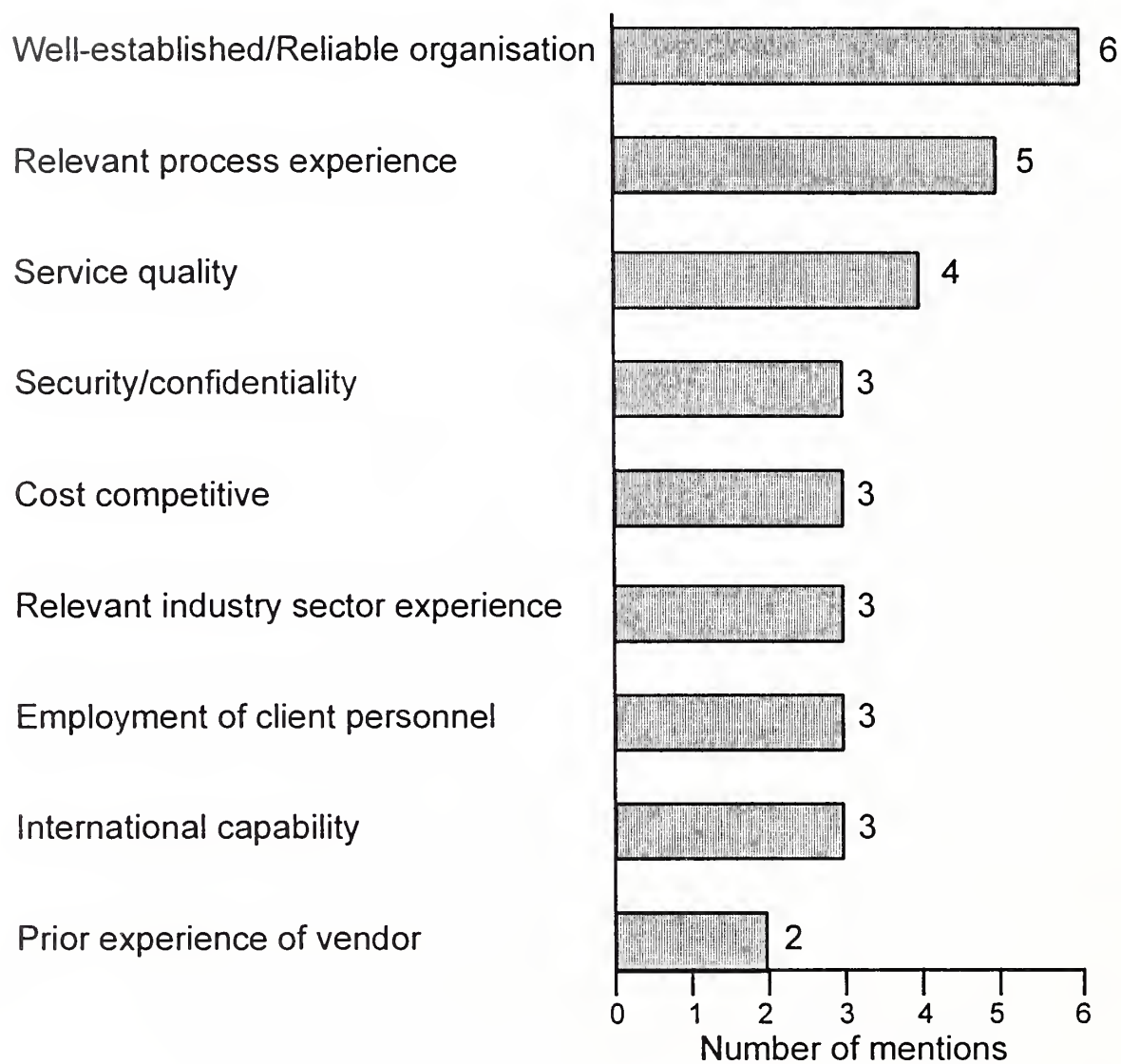
C

Process Experience is Critical

Exhibit III-9 lists the vendor selection criteria which were most frequently mentioned by respondents.

EXHIBIT III-9

Vendor Selection Criteria Business Operations, Europe



Sample of 37 respondents

As in IS outsourcing, vendor stability is a very important criterion. Users need to be certain that the chosen vendor will continue to serve their needs reliably over the life of the contract. However, at present, many of the business functions being outsourced are broadly applicable to a range of industries. Accordingly, users perceive process expertise to be more important than knowledge of their industry sector.

Service quality and cost are obviously very important. However, another important attribute is confidentiality. Buyers are handing over the operation of part of their business to a vendor and do not expect information to be disclosed to their competitors. Despite the propensity to outsource low security activities such as catering and buildings maintenance, business operations activities can be a significant source of competitive advantage. For example, Vauxhall has outsourced elements of its customer assistance service to EDS. This function is a potential source of competitive advantage to Vauxhall and the company is reluctant to disclose details of this operation.

As with IS outsourcing, many buyers would like to transfer the staff previously associated with the business function to the business operations' vendor.

Buyers were also asked to rate the importance of each of the potential vendor characteristics shown in Exhibit III-10.

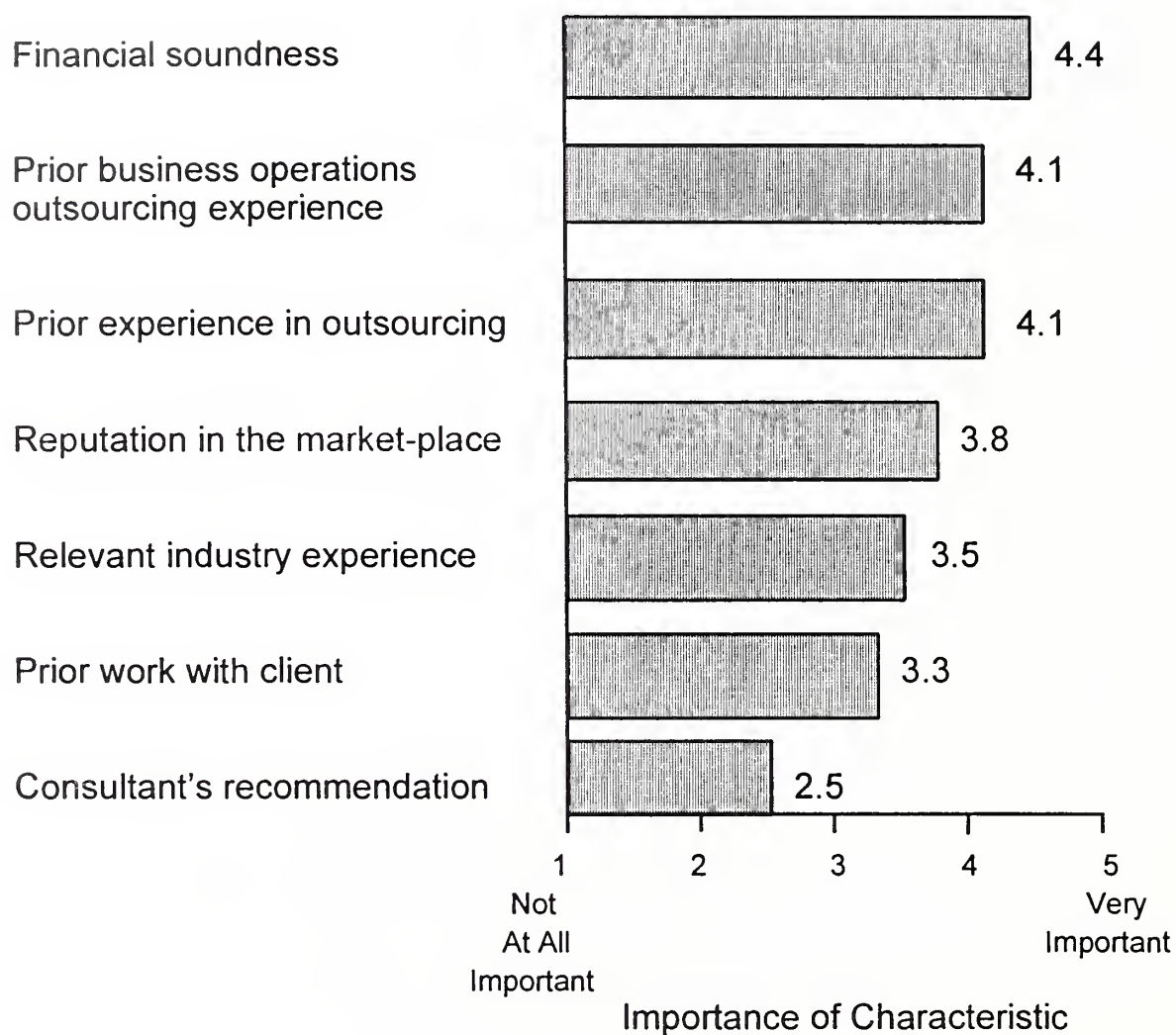
Essentially vendors need to demonstrate that:

- They will be active in business operations for a period well in excess of the proposed contract term
- They are financially secure
- They have capability and experience in handling outsourcing-style relationships
- Business operations outsourcing is a key element of their business strategy.

Ideally, buyers expect vendors to demonstrate prior outsourcing capability, preferably with services that go beyond IS outsourcing.

EXHIBIT III-10

Required Vendor Characteristics Business Operations, Europe



Sample of 36 respondents in France, Germany and the U.K.
Standard error = 0.15.

D**Buyers Favour Professional Services Vendors**

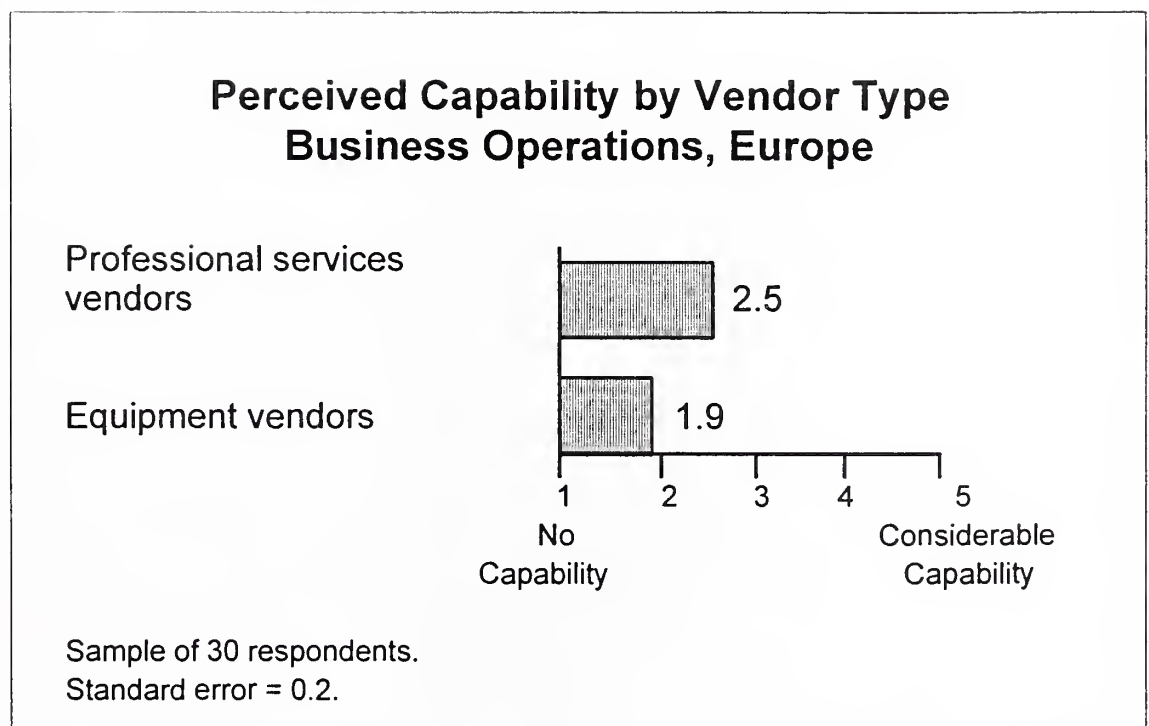
Overall, buyers exhibit low levels of enthusiasm for transferring the management and operation of non-IT business functions to IT vendors.

Many respondents perceive that IT vendors lack relevant skills outside the IT domain. Furthermore, senior executives are typically unimpressed with the contribution that IT has made to the development of their organisations. Many still perceive IT vendors to be primarily technologists with inadequate levels of understanding of their clients' businesses.

Accordingly, the ratings of the business operations capabilities of all of the IT vendors mentioned in the survey were low.

Exhibit III-11 shows the average ratings received by professional services vendors and equipment vendors.

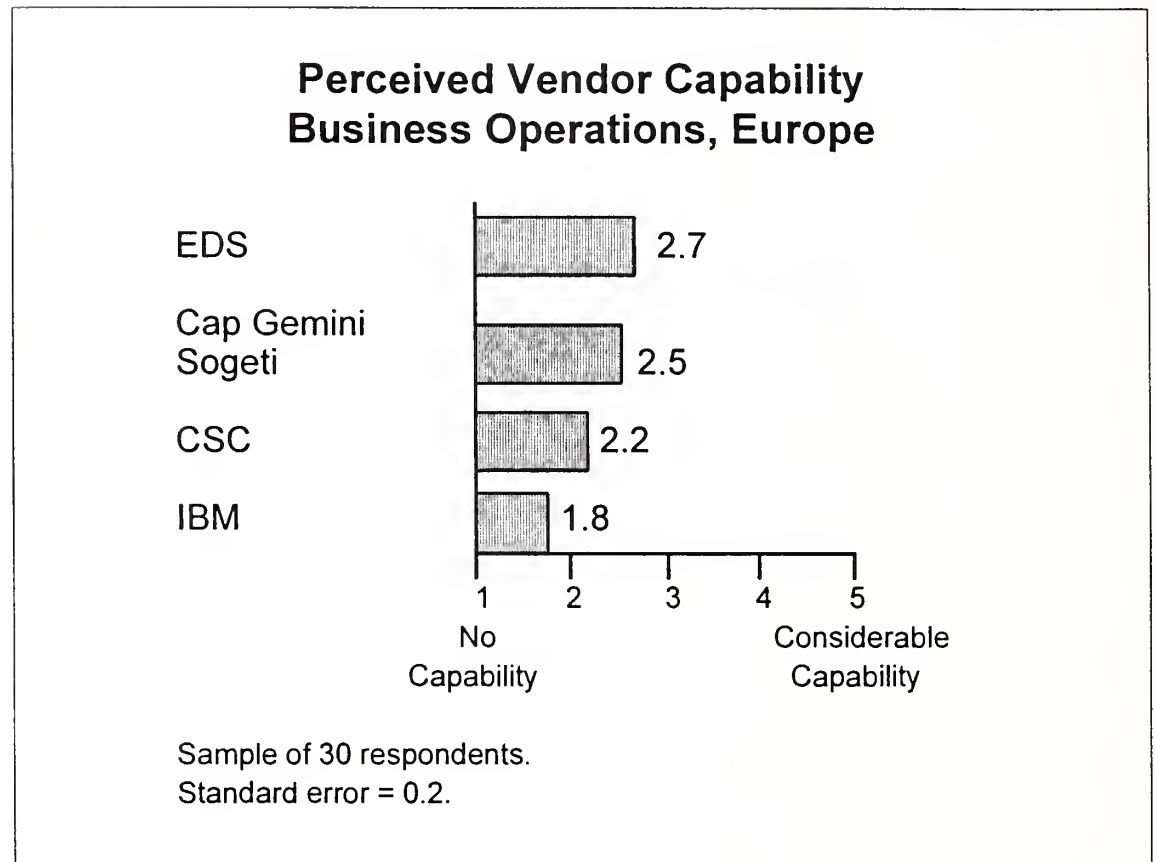
EXHIBIT III-11



Overall, the equipment vendors received consistently lower scores than the professional services vendors in France and the United Kingdom. The notable exception to this pattern is Siemens Nixdorf Informationssysteme, which was rated in second place behind EDS in Germany.

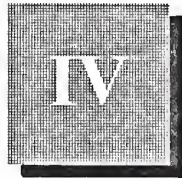
Exhibit III-12 shows the ratings achieved by four individual vendors.

EXHIBIT III-12



EDS was the most highly rated organisation amongst the four listed in the exhibit. This is probably to be expected because EDS arguably has the highest level of business operations outsourcing experience within this group.

However, to state that EDS is unequivocally regarded as the vendor with the highest level of business operations capability in Europe would be unfair to Andersen Consulting. Andersen Consulting is not included in Exhibit III-12 because attitudes towards Andersen were only researched in the United Kingdom, where the organisation is more highly rated than EDS. In addition, Andersen Consulting was mentioned by approximately 40% of respondents in France in spite of their exclusion from the survey there.



Country Characteristics

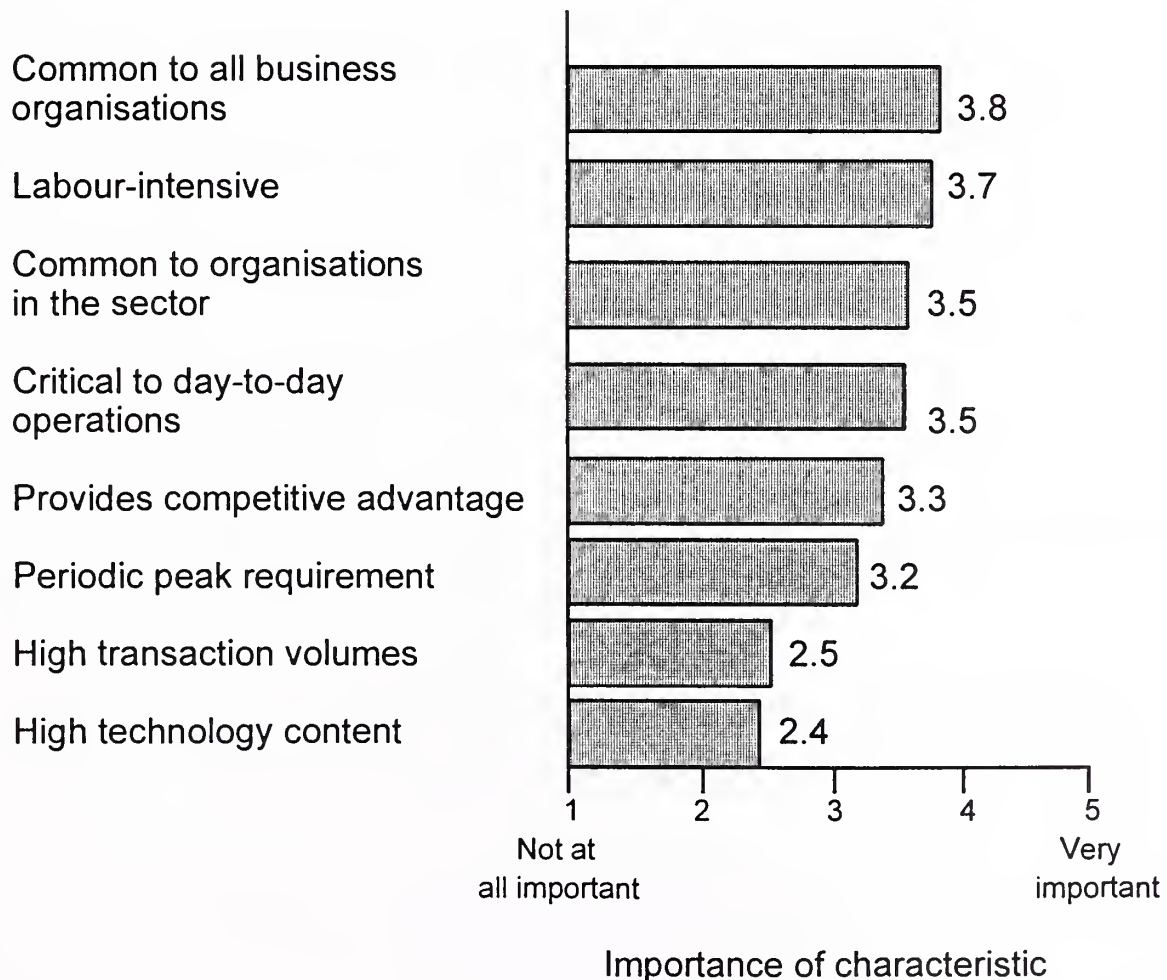
A

Labour Intensity is an Important Factor in the U.K.

Exhibit IV-1 lists the U.K. ratings for potential characteristics of business operations candidates.

EXHIBIT IV-1

Principal Characteristics of Business Functions to be Outsourced, United Kingdom



Sample of 15 respondents.
Standard error = 0.2.

There is a strong requirement to reduce the numbers of internal personnel within U.K.-based organisations. Vendors are advised to target activities that are strongly labour-intensive. However, buyers also show a propensity to outsource activities which have a low technology content rather than a high technology content.

This poses a significant challenge to IT vendors. The implication is that vendors need to identify activities which are currently labour-intensive, but where they will in future be able to increase efficiency significantly through use of information systems.

Given this scenario, vendors have a choice of offering. They can adopt one of two approaches, namely:

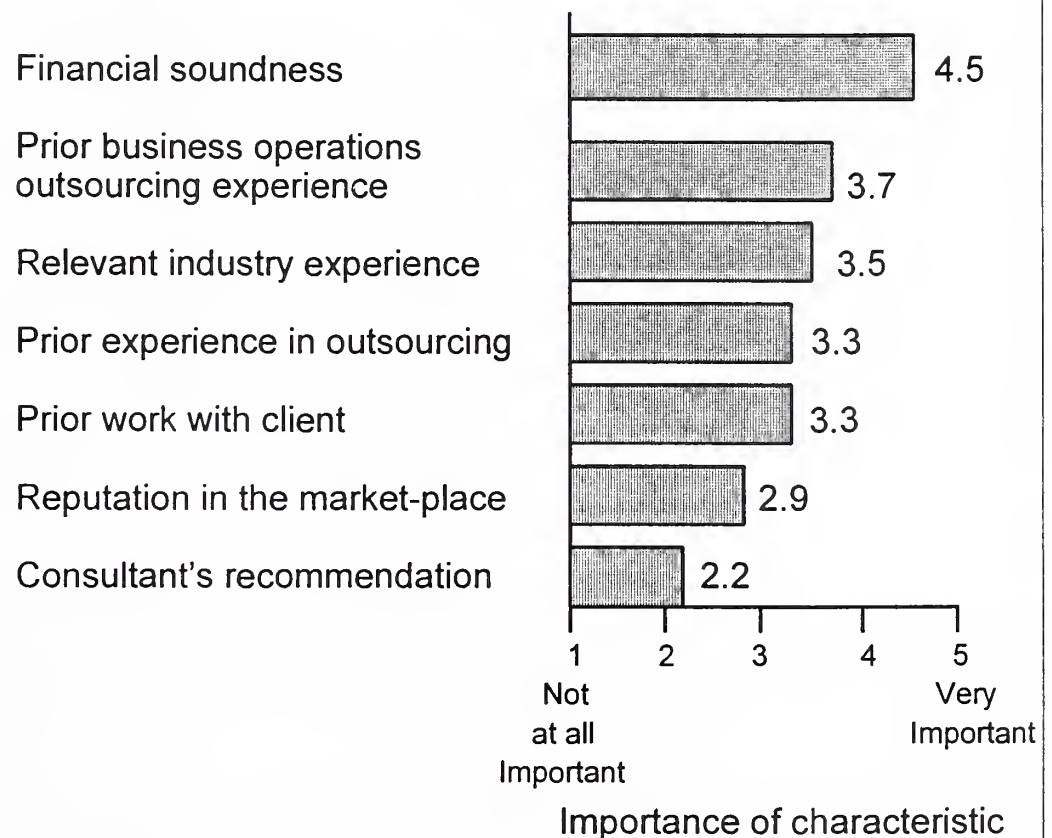
- Suggesting a systems integration project to re-engineer the activity and introduce new technology
- Suggesting a business operations approach.

The client organisation may be faced with the need to redeploy, or make redundant, significant numbers of staff if the systems integration approach is adopted. Adopting a business operations approach potentially transfers this problem to the vendor. This may be more acceptable to the client.

Exhibit IV-2 lists the U.K. ratings for a number of vendor characteristics.

EXHIBIT IV-2

Required Vendor Characteristics Business Operations, United Kingdom



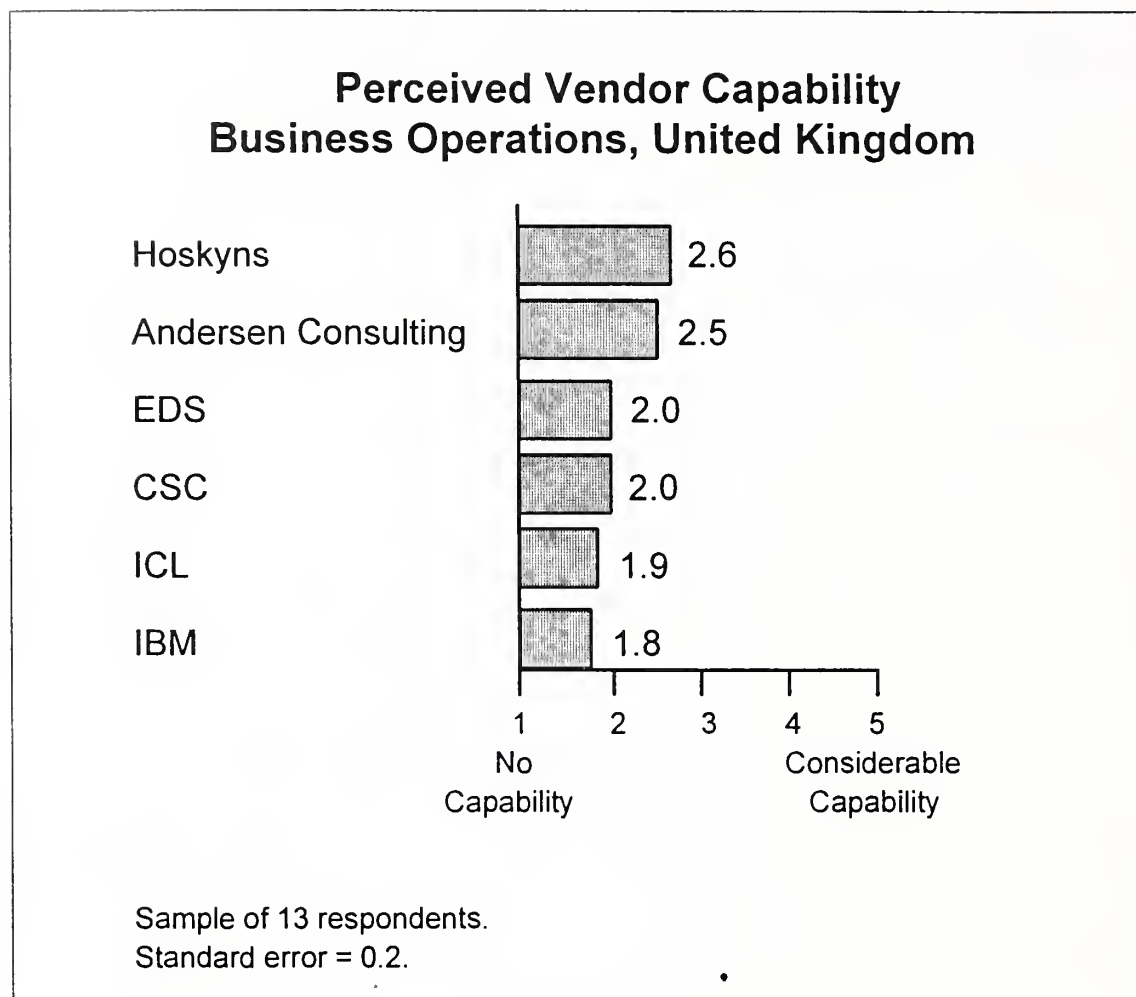
Sample of 15 respondents.
Standard error = 0.2.

Financial solidity is of overwhelming importance in the United Kingdom. This implies that it will be difficult for small to medium-sized vendors to establish themselves in business operations outsourcing.

In addition, buyers now expect vendors to have prior experience in business operations outsourcing. This expectation mirrors the situation in the U.K. public sector. Here vendors are finding it difficult to compete in the outsourcing market unless they have built up, or acquired, a business operations capability.

Exhibit IV-3 lists the perceived business operations capability of a number of potential vendors in the United Kingdom.

EXHIBIT IV-3



The leading business operations vendors serving the local government sector in the United Kingdom are Capita Group and CSL. CSL has recently been acquired by the accountancy organisation Touche Ross. These vendors were not included in the survey, because it was targeted at business operations outsourcing in the commercial sector.

Overall the ratings are very low, indicating a perception of inadequate business operations capability for each of these vendors. However, this situation can change rapidly in an emerging market.

The two vendors perceived to have the highest levels of capability are Hoskyns and Andersen Consulting.

Andersen Consulting has been targeting business operations opportunities in the United Kingdom for several years. Andersen has a well-publicised contract to manage accounting services for BP Exploration in Aberdeen. This service has now been extended to two other organisations operating in the North Sea oilfields - Sun Oil and Azco.

In addition, Andersen Consulting perceives that there is currently considerable interest in business operations outsourcing in the U.K. Andersen is believed to be about to announce two more business operations contracts. One of these involves the operation of the customer service function for a major consumer goods supplier. Andersen Consulting will accept mailed or phoned orders from agents and perform all activities through to despatch of the goods. The other contract is believed to include blue collar as well as white collar functions.

Andersen Consulting perceives that any white collar function employing a significant number of people is a legitimate target for business operations outsourcing. The most promising opportunities for Andersen Consulting are organisations seeking radical business change.

EDS receives a low rating in the United Kingdom. However, the company does already have a number of business operations contracts here, notably:

- Fulfilment activities for Time Life
- Customer assistance services for Vauxhall
- Parking fine administration in London.

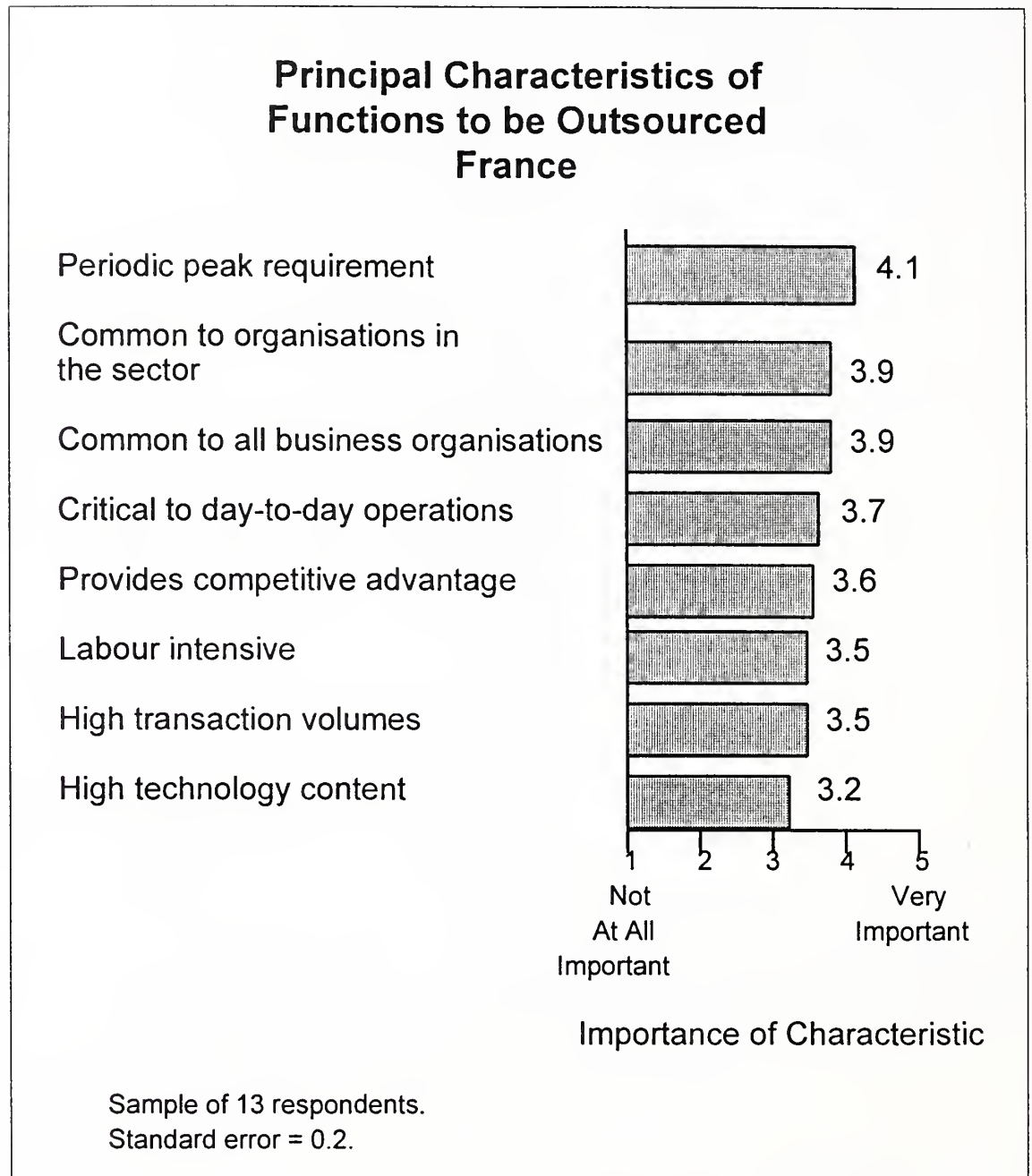
IBM ISL also claims to be targeting business operations contracts. CSC does not appear to be targeting business operations in the United Kingdom at present.

B

Periodic Activity is an Important Factor in France

Exhibit IV-4 lists the ratings given to potential characteristics of business operations candidates by respondents in France.

EXHIBIT IV-4



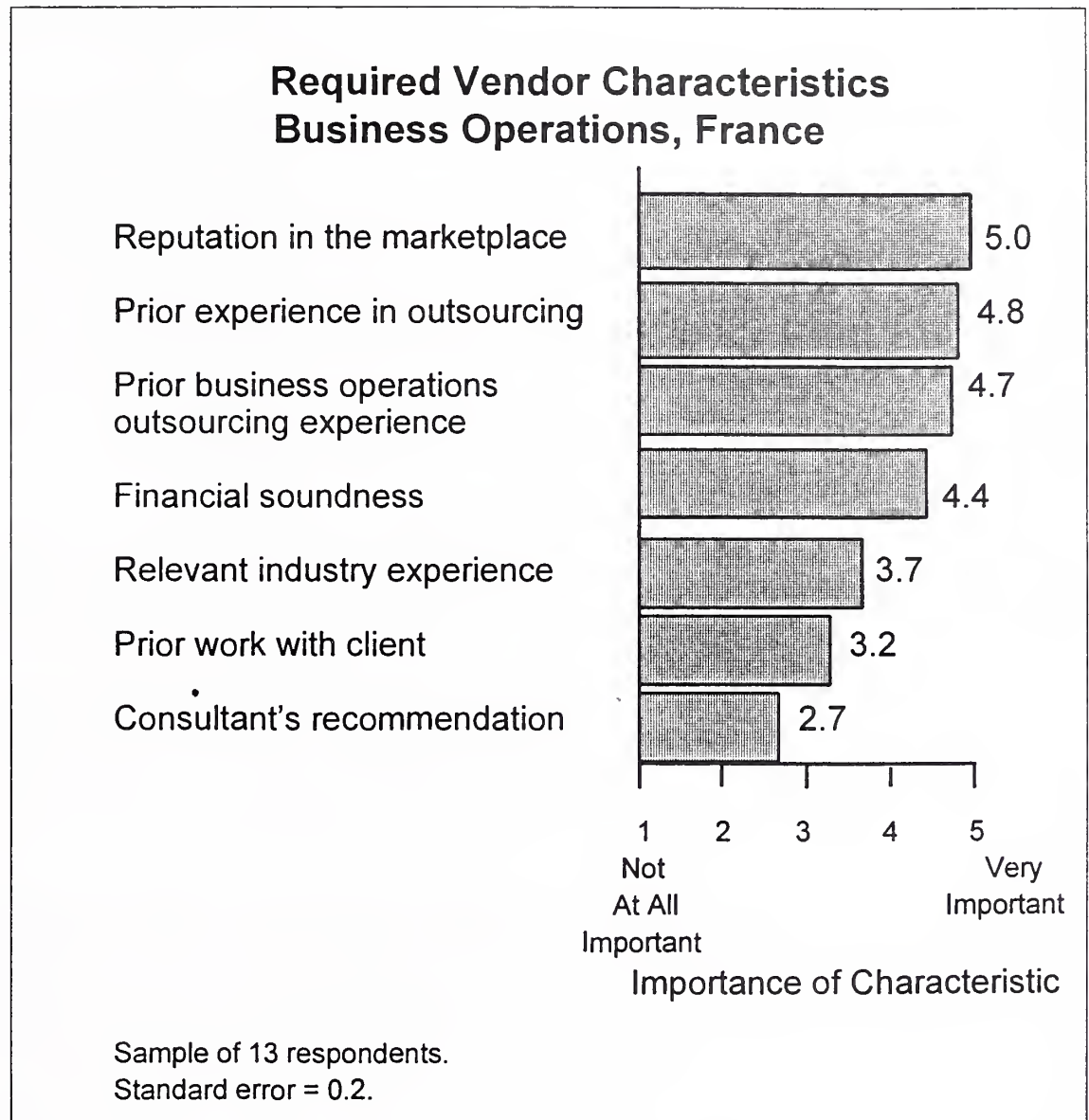
Overall, the level of ratings in France is noticeably higher than that in the United Kingdom, potentially indicating a higher level of enthusiasm for the concept of business operations outsourcing.

The pattern of relative importance of each of these characteristics is similar in France and the United Kingdom with two exceptions. Firstly, the labour-intensity of an activity is a relatively less important factor in France than in the United Kingdom. Secondly, functions with periodic peak levels of activity are more favoured for outsourcing in France than in the United Kingdom.

This implies that organisations in France will tend to outsource functions with highly variable levels of activity while organisations in the United Kingdom will outsource business functions to reduce their staffing levels.

Exhibit IV-5 shows the relative importance of potential characteristics of business operations vendors in France.

EXHIBIT IV-5



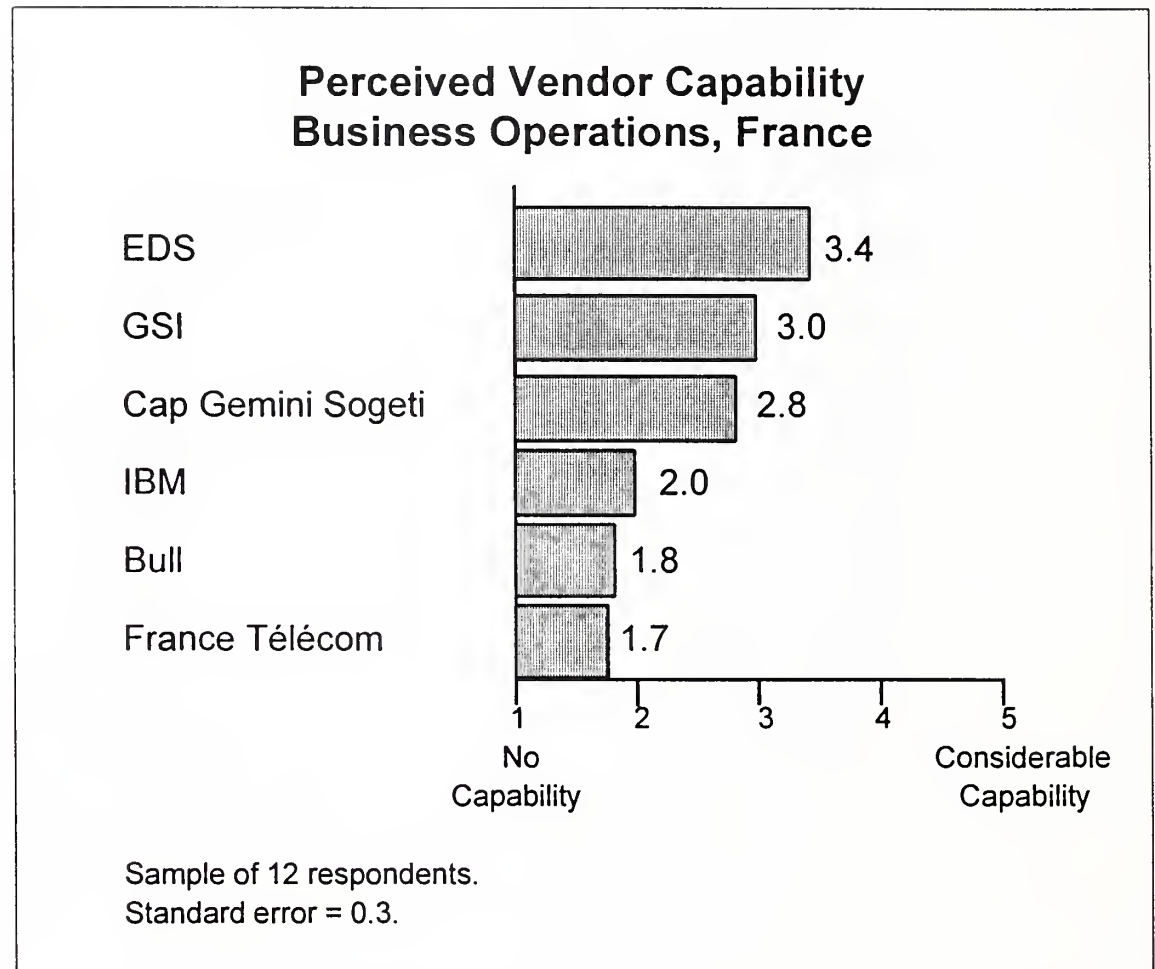
It is very important in France that vendors demonstrate prior experience in business operations. This will tend to favour:

- Vendors with international business operations experience such as EDS
- Local vendors with specialised experience such as bank card processing.

Accordingly, companies such as GSI and Axime, which offer specialised services to the banking and finance sector, are well placed to take advantage of the trend towards business operations outsourcing and extend their activities in this sector.

Exhibit IV-6 lists the perceived business operations capability of a number of potential vendors in France.

EXHIBIT IV-6



In addition to the vendors shown in the exhibit, Andersen Consulting received a high number of mentions as a potential supplier in France. This implies that Andersen Consulting would have been given a comparatively high rating for its business operations capability had the organisation been included in the French research.

EDS received the highest rating in France. EDS perceives that the traditional software and services market is becoming very highly competitive. Accordingly, EDS wishes to extend its offerings beyond software and services into more extensive business functions.

The company currently appears to be targeting a number of business operations opportunities, namely:

- Parking applications
- Customer assistance centres
- Document management.

EDS has already signed two contracts—in Seville and London—to administer parking fine collection, in addition to its contract in Chicago.

Seville City Council has signed a four-year outsourcing contract with EDS to design, construct and administer a traffic offence system.

The contract is performance-related with EDS committing to increase the percentage of parking tickets paid.

EDS is also intending to target customer service operations in Europe. At present the company has two contracts of this type in Europe.

Firstly, the company runs customer assistance centres on behalf of GM subsidiaries, including Vauxhall in the United Kingdom. Vauxhall is reluctant to discuss the nature of this contract, believing that it confers an important competitive advantage on their organisation. The contract essentially involves manning a customer service hotline and assisting Vauxhall in maintaining high levels of customer satisfaction, via effective handling of customer complaints. In addition, the information gathered is channelled back into Vauxhall's ongoing marketing and product development.

Secondly, EDS is managing the logistics function on behalf of Time Life.

EDS' Customer Services Technology Division will become increasingly active in areas such as these. In the U.S., this division has already designed and implemented a customer recovery programme on behalf of AT&T. EDS is paid for each defecting customer it recovers in this case.

EDS also sees an opportunity to take over the administration of claims functions where large volumes of paperwork are involved. In particular, EDS will endeavour to target insurance claims processing with business operations contracts based around document image processing technology.

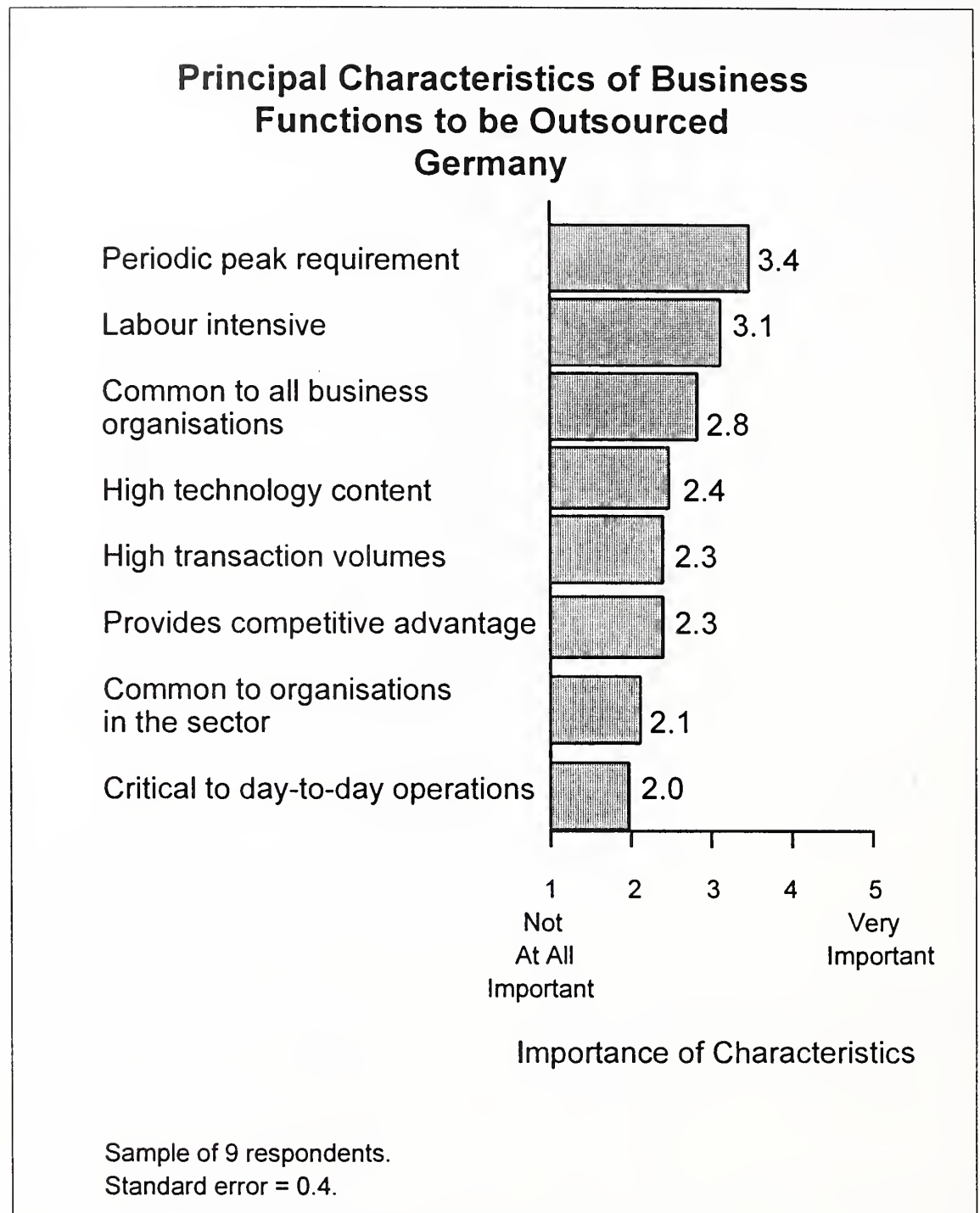
C

SNI Perceived to Match Service Vendor Capability in Germany

Exhibit IV-7 lists the ratings given to potential characteristics of business operations candidates by respondents in Germany.

Overall the level of ratings in Germany is significantly lower than those in the United Kingdom and France, indicating a comparatively low level of enthusiasm for business operations outsourcing.

EXHIBIT IV-7



Organisations in Germany are most inclined to outsource business functions which

- Exhibit highly variable levels of activity
- Are labour intensive.

However, compared to organisations in France and the United Kingdom, organisations in Germany are reluctant to outsource business functions which are common, but possibly critical, to organisations in their sector. Organisations in Germany are most likely to outsource activities which are common to all organisations, not just those in their sector.

Overall organisations in Germany are currently disinclined to outsource business functions that

- Provide competitive advantage
- Are critical to their day-to-day operations.

Exhibit IV-8 shows the relative importance of potential characteristics of business operations vendors in Germany.

EXHIBIT IV-8

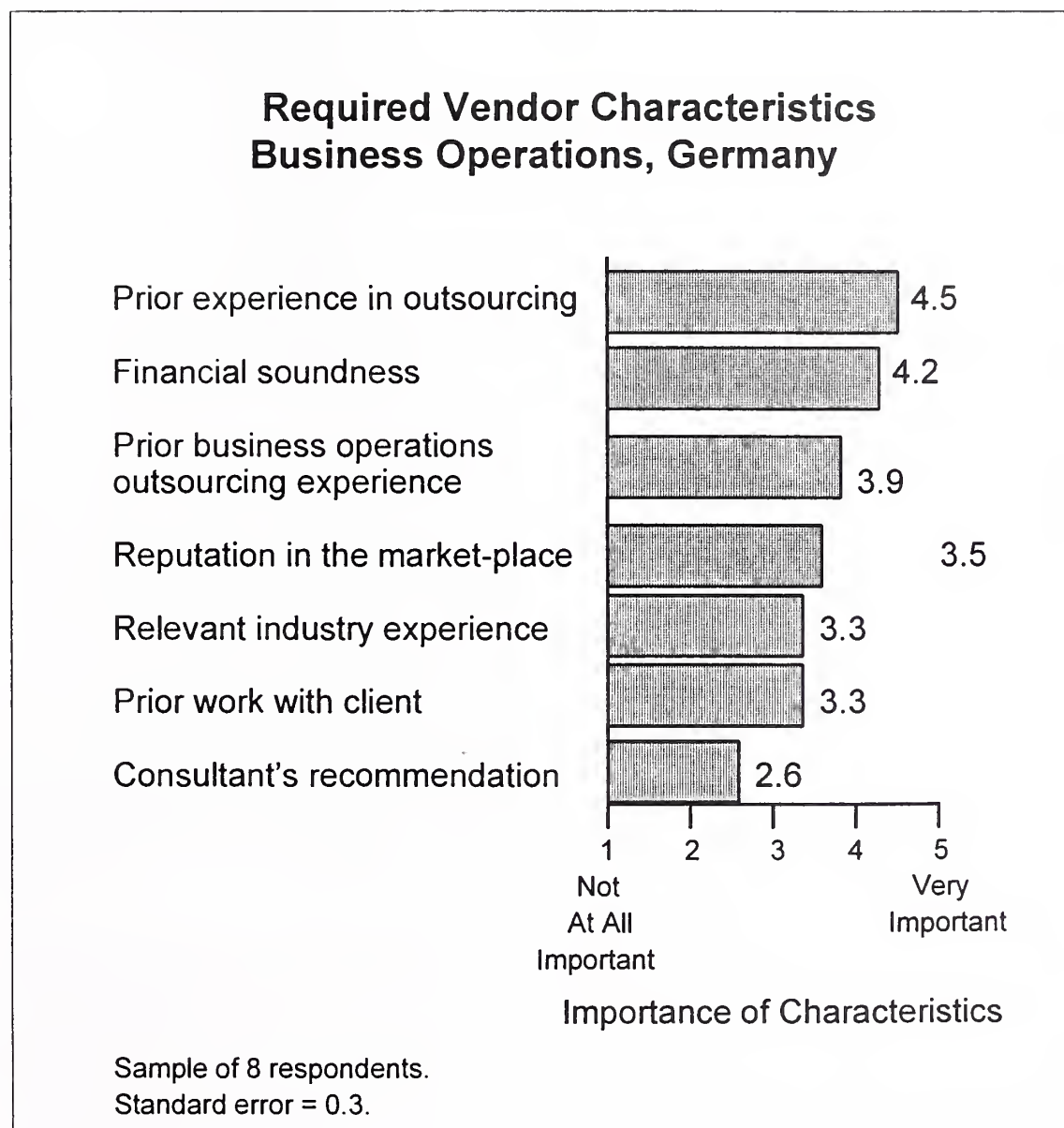
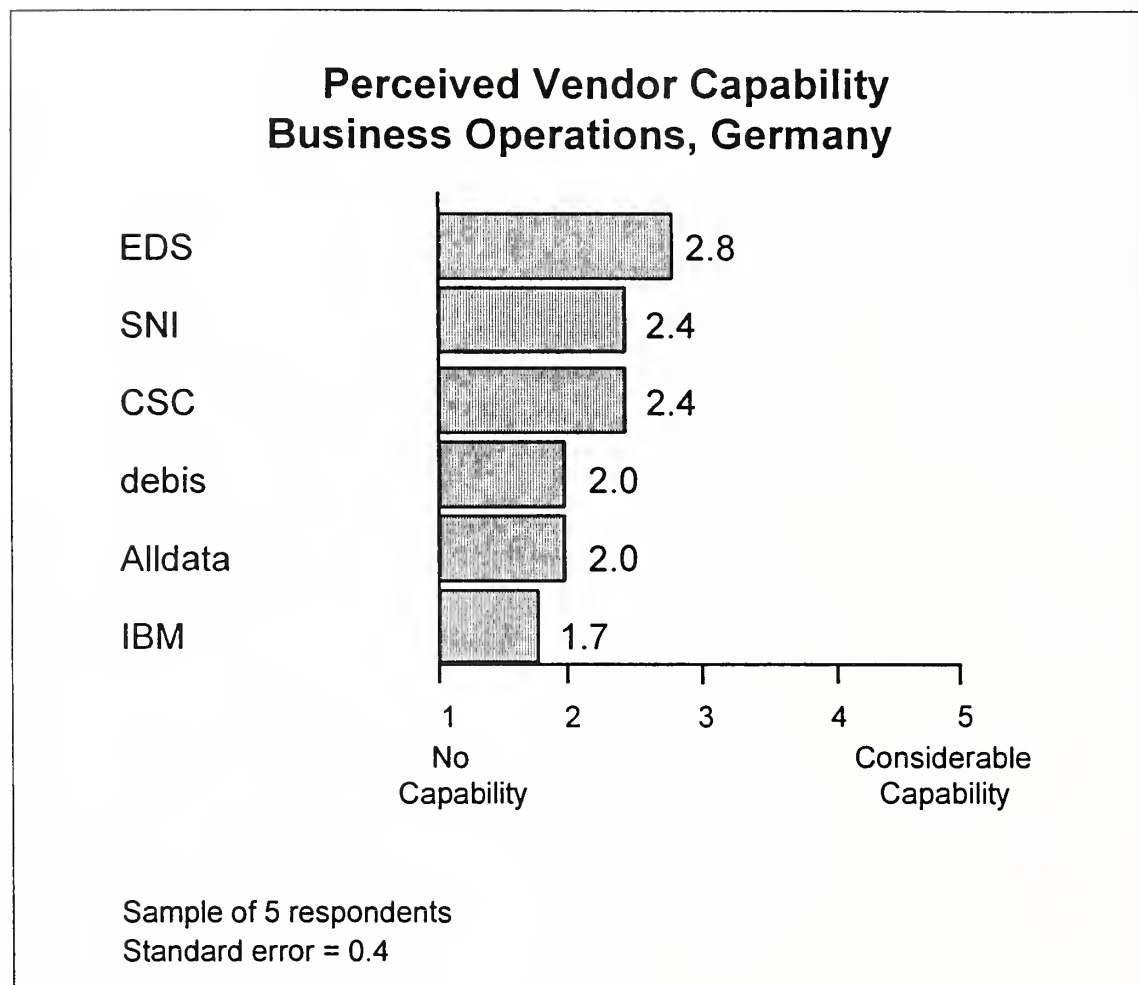


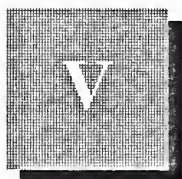
Exhibit IV-9 lists the perceived level of business operations capability of a number of potential vendors in Germany.

EXHIBIT IV-9



As in France, EDS is the most highly rated vendor, but with a perceived lower capability than in France. IBM receives a low rating in Germany, giving the company a consistently low score in terms of its perceived business operations capability across Europe.

However, Siemens Nixdorf Informationssysteme received a rating equal to that of CSC and greater than that of debis Systemhaus. This makes SNI the only equipment manufacturer, amongst IBM, SNI, ICL and Groupe Bull, to outscore a major professional service vendor in terms of perceived business operations capability.



Case Studies

A

BP Exploration Optimises the Process, not its Components

One of the earliest examples of business operations outstanding in Europe is Andersen Consulting's contract with BP Exploration to take over the operation of the company's accounting function in Aberdeen. This contract was signed in June 1991 and is valued at £55 million over four years.

In 1990, BP Exploration was faced with the following scenario for its North Sea operations:

- Oil price falls in real terms
- Costs rising as a result of:
 - An increasing number of small oilfields
 - Growing environmental pressures.

Accordingly, the organization reviewed all of its activities to identify means of possible cost reduction. Many activities were outsourced as a result.

BP Exploration perceived that the bulk of the accounting function in Aberdeen could be outsourced, provided that BP Exploration remained in charge of business interpretation, setting policy and establishing standards of service.

Accordingly, BP Exploration transferred 310 personnel to Andersen Consulting, retaining 30 to 40 members of the original accounting department. These staff were merged with planning personnel, forming a new commercial department.

BP Exploration did not go out to competitive tender for this contract. The company had a long relationship with Andersen Consulting, and were impressed by Andersen Consulting's ethos, overall capabilities and systems expertise. However, the deciding factors in choosing Andersen Consulting were the perceptions that the two organizations shared the same vision and were culturally compatible. BP Exploration believes that getting the cultural aspects of an outsourcing relationship right is more important than cost.

BP Exploration could have optimised contract costs by separately outsourcing:

- Equipment operation
- Software development and maintenance
- Accounting services.

However, instead the company wished to provide scope for its chosen supplier to re-engineer the overall business process. BP Exploration perceived that Andersen Consulting had the capability to do this and manage all aspects of the process.

BP Exploration is pleased with the progress that has been made. The company has been the beneficiary of 20% cost savings and its management has been freed to focus on important business issues rather than day-to-day administration of the accounting department.

To achieve improved quality of service, Andersen Consulting has consolidated BP Exploration's accounting activities from six sites to a single site. In addition, the software has been modified to speed up processes and service transferred to equipment based in Andersen Consulting's Harrogate centre.

The business activities performed by Andersen Consulting include:

- Processing of invoices and payments
- Management of bank accounts
- Production of monthly and quarterly management reports and identification of variances
- Production of statutory accounts.

Andersen Consulting is measured against service level agreements based on daily, weekly and monthly deliverables. BP Exploration is particularly concerned about accuracy in maintenance of bank accounts, and on-time payment of invoices.

Performance is reviewed via a monthly performance report. However, BP Exploration stresses the importance of client and vendor working together to improve the overall service and not using review meetings to apportion blame.

The price of the contract is reviewed quarterly in advance. A global fee is agreed which moves with the level of activity but is not priced by item.

B**Time Life Outsources Fulfilment to EDS**

Time Life operates three book clubs in Europe. Business is derived mainly from the United Kingdom because all the publications are in English, but a significant volume of business comes from elsewhere in Europe.

The principal business functions for Time Life are:

- Marketing, including advertising and direct mail
- Warehousing and distribution
- Fulfilment.

Time Life still performs the marketing, warehousing and distribution functions in-house but has awarded a business operations contract to EDS covering its fulfilment activities.

The functions performed by EDS within this contract include:

- Capturing and processing all incoming mail (approximately four million items per annum)
- Processing new enrolments
- Processing customer orders and payments
- Maintaining customer accounts.

Perhaps surprisingly, Time Life still manages and operates its own mainframes and EDS provides a daily update of transactions to these mainframes each evening.

EDS is paid a fixed rate per item processed by Time Life. However, EDS's cost structure to perform these activities on behalf of Time Life is predominantly fixed cost. Accordingly, EDS would like to increase the profitability of this operation by taking on other similar business operations contracts which could share its existing facilities.

EDS is also aiming to re-engineer the business processes in the medium-term to reduce costs. At present, many of the activities performed are labour intensive. EDS believes that it can introduce higher levels of automation to reduce costs. Examples of applicable technologies include:

- Automatic letter opening equipment
- Scanning and document image processing.

C

Processing Services Become Business Operations Outsourcing

A number of suppliers of bureau services have begun to extend their offerings beyond computer processing to handle wider aspects of a business function.

Two notable examples of this trend are:

- Payroll administration
- Share registration.

Payroll services traditionally depended on the client either keying data into a personal computer or completing rigidly defined data input forms. Accordingly, much of the payroll administration was still performed by the client rather than the processing services vendor.

However, vendors are now targeting a wider range of payroll office functions, such as

- Pre-processing of data into a form suitable for data input handling employee queries
- Liaison with Inland Revenue
- Provision of management information, for example analyses of employee absences.

Such services can be tailored to the demands of the client. At one extreme, the service can be shrink-wrapped into standard form to provide a low-cost option for small organizations. A more tailored service, possibly involving on-site front-office functions, can be offered to larger organizations. Similarly, pricing can be based on either a fixed charge or related to the number of personnel on the payroll.

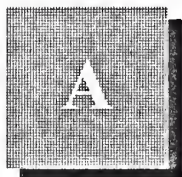
There is potential to extend the scope of most processing services in a similar way. For example, CMG has offered a bureau service covering share registration for 20 years.

However, the company has recently extended the scope of this service for two clients: BP and Grand Metropolitan.

In the case of BP, CMG acquired 60 personnel from BP's in-house share registry operation. CMG now supplies all share registration services to BP including:

- Shareholder queries
- AGM administration
- Dividend fund administration
- Administration of lost certificates and deaths.

CMG now wishes to develop these activities to include a wider range of investor services.



User Questionnaire

Business Operations Outsourcing

Good Morning (Afternoon). This is _____. I'm calling from INPUT, a leading market research firm in the field of information services.

INPUT needs your assistance in identifying issues and market potential for the area called business operations outsourcing. INPUT's definition of business operations outsourcing is the turning over to the vendor management of an entire functional process in an organization, either financial, human relations or some other function. You need not be outsourcing a business operation currently to respond to our survey.

We appreciate your assistance and, in return, we would like to send you a copy of the executive overview of the report when it is completed.

The questions will take about 15 minutes. Is this a good time to discuss this or would you prefer to schedule a specific time for me to call back?

Now (Go to next page)

Later _____ (time and date)

1. Has your organization outsourced any of its information systems operations to a vendor?

Yes _____

No _____ (Go to 5)

2. Which of the following IS functions have been outsourced to a vendor and who is the vendor?

Function	Vendor	
a. Processing Operations	_____	_____
b. Applications Maintenance	_____	_____
c. Applications Development	_____	_____
d. Network Management	_____	_____
e. Desk Top Services	_____	_____
f. Business Operations	_____	_____

(If the response to 2f was yes, ask the following question, else go to 5).

3. You indicated above that you already outsource some business functions. What are they and why were they outsourced?

Function	Why?
_____	_____
_____	_____
_____	_____
_____	_____
_____	_____
_____	_____

4. Again, let's consider the business functions you have outsourced.

a. What criteria did you use in selecting a vendor?

b. Who was selected and why? _____

c. What was the contract value and length?

•
\$ _____

_____ years

d. How do you manage the contract?

5. Do you plan on outsourcing any (other) business operations in the next five years? If so, which functions are candidates and when will they be outsourced?

No _____ (go to 6)
Yes _____

Function	When
_____	_____
_____	_____
_____	_____
_____	_____

6(a). The following is a list of characteristics of a business operation. How important is each of these, on a scale of 1 to 5 in making the business operation a candidate for outsourcing?

<i>Process</i>	<i>Circle one</i>
Common to organizations in your industry	1 2 3 4 5
Common to all business organizations	1 2 3 4 5
Labor intensive	1 2 3 4 5
High technology content	1 2 3 4 5
High transaction volumes	1 2 3 4 5
Periodic peak requirement	1 2 3 4 5
Critical to day to day operations	1 2 3 4 5
Provides competitive advantage	1 2 3 4 5

(b) What other factors are important?

7. In your opinion, which of the following vendors have the capability to take over the responsibility for business operations? Please score their capability on a scale of 1 to 5, where 1 = no capability and 5 = considerable capability.

_____	_____
_____	_____
_____	_____
_____	_____
_____	_____

8. What would you look for in a vendor that you can outsource your business operations to? Please rate the following factors on a scale of 1 to 5, with 5 being the most important.

	Circle one
Experience in your industry	1 2 3 4 5
Prior experience in outsourcing	1 2 3 4 5
Prior business operations outsourcing experience	1 2 3 4 5
Prior work with your company	1 2 3 4 5
Reputation in the market place	1 2 3 4 5
Recommendation from a consultant	1 2 3 4 5
Financial soundness	1 2 3 4 5

9. In your opinion, what do you think would increase the appeal of business operations outsourcing for prospect organizations?

10. On a scale of 1-5, how likely is your organisation to outsource the management and operation of a non-IT business function in the next two years? _____

Thank you for your cooperation on this project. If I can verify your address, I will make certain you get a copy of the executive overview to this report when it is released.

Name _____

Title _____

Company _____

Address _____

City _____

State/Zip _____

Phone No. _____

